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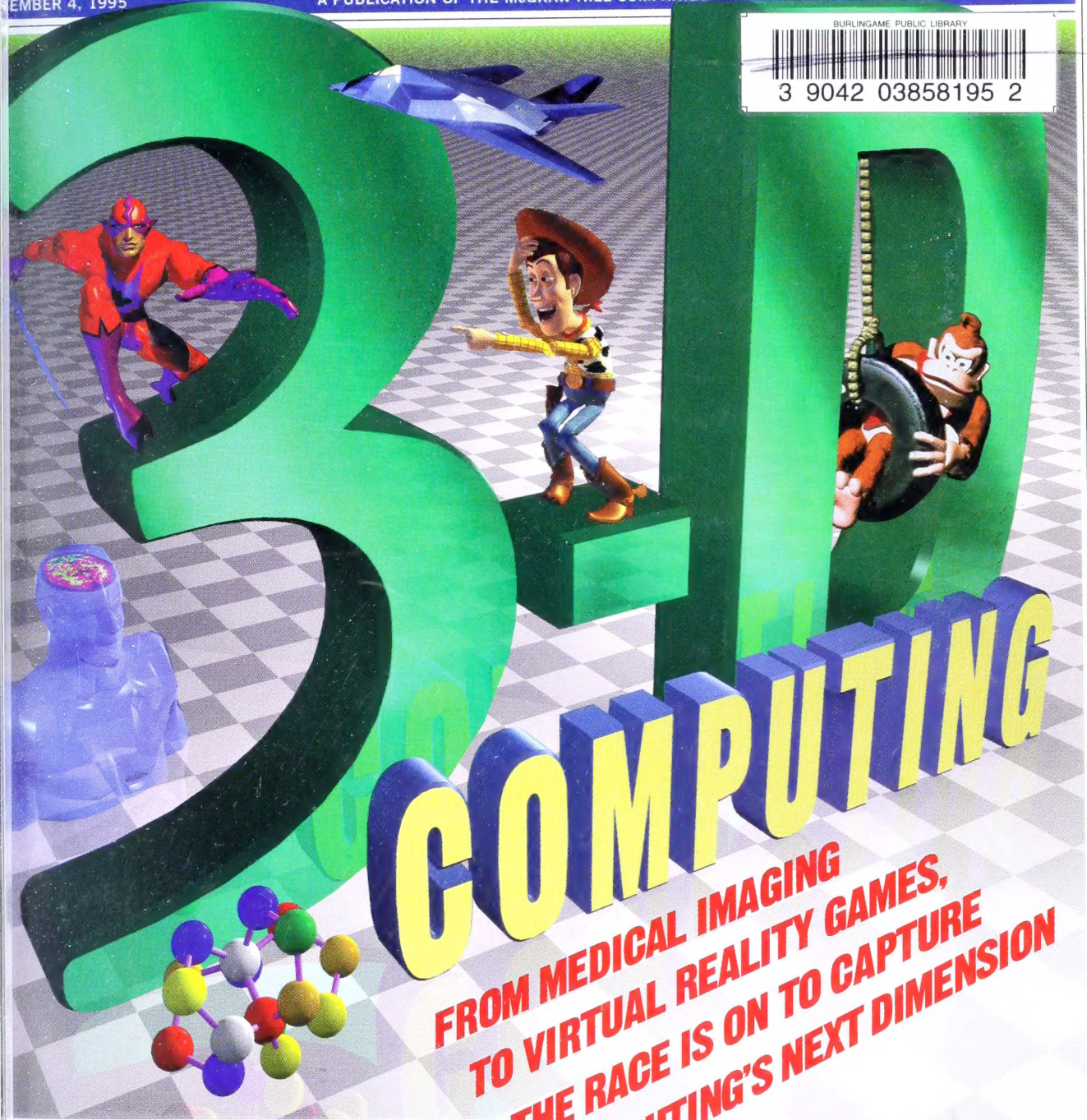


AL ESTATE MOMENTUM PICKS UP CHINA ON TAIWAN LAWSUITS HASHING OUT A NEW DEAL

SS WEEK  
September 4

# BusinessWeek

EMBER 4, 1995 A PUBLICATION OF THE MCGRAW-HILL COMPANIES \$2.95



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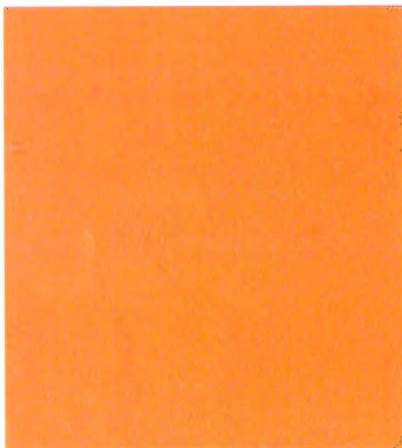
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™

Windows® 95





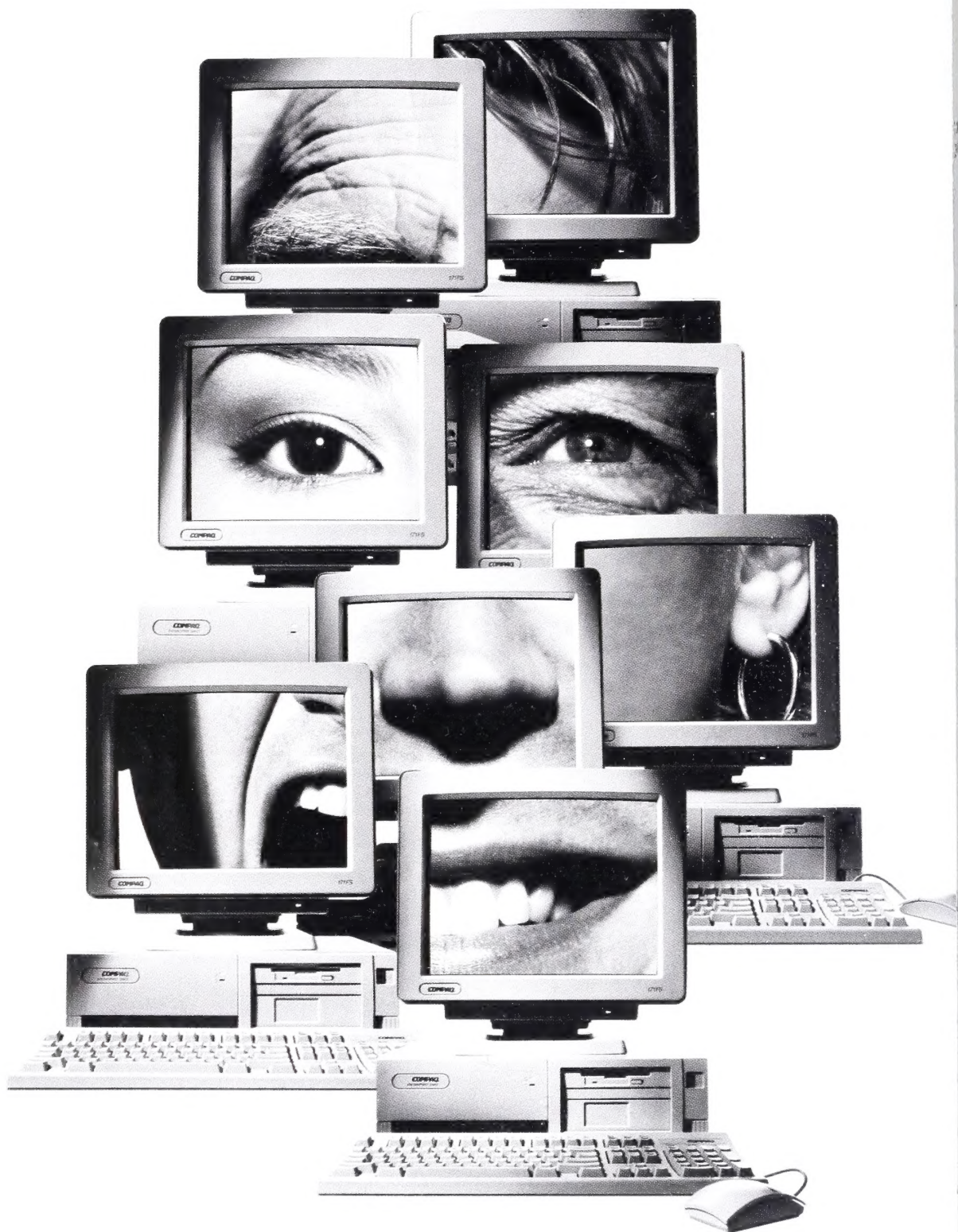
Windows 95 can help your computer grow by making it effortless to immediately begin using new Plug-and-Play peripherals.

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# BusinessWeek

SEPTEMBER 4, 1995

**COVER STORY**  
3-D computing is science fiction anymore—and tech companies big and small are grappling for a piece of the fast-growing pie  
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## Cover Story

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The Defense Dept. uses it for simulated war games. Scientists have toyed with it for years. Now, three-dimensional imaging is fast making its way to work and home PCs—and it isn't limited to virtual reality. Thanks to ever-cheaper and more powerful computers and plunging prices for equipment, it's a whole new dimension for everything from oil exploration to architecture to moviemaking

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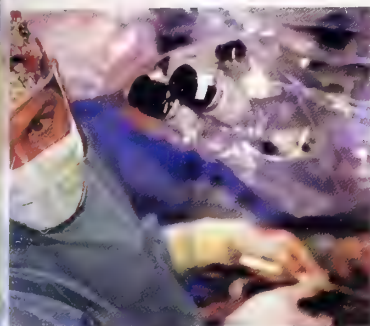
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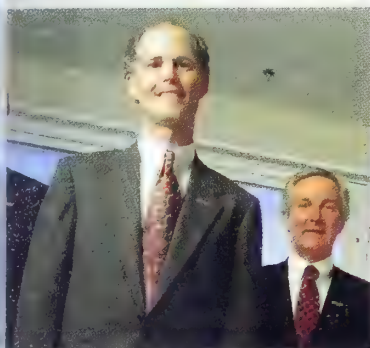
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Clinton successfully courted Big Business in '92. But for '96, he'll find it increasingly as the enemy



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procedures may become less invasive, thus less painful and less expensive page 32



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## Workplace

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In the middle of a lockout, dissident players try to scrap the union. The union is at risk

**PAY SOARS CLEAN OUTTA SIGHT**  
The global reach of technology means talent earns more than ever

## Corporation

**WHEELER-DEALER HEALER...**  
Columbia/HCA is swallowing hospitals and right, cutting staff, cutting costs—and cutting doctors in  
**AND THE PATIENTS LEFT BEHIND**  
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**LAST-IMPLANT FINALE?**  
As a deadline approaches, all parties have a huge stake in a single settlement, rather than thousands of jury trials

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# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

## CORPORATE COUPLINGS

### HONDABISHI MAY BE AROUND THE CORNER

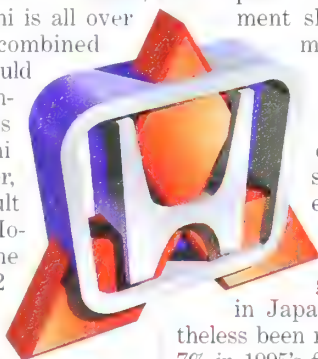
ARE HONDA AND RIVAL AUTO maker Mitsubishi merger-bound? Despite the companies' vehement denials, that's the buzz among Tokyo auto watchers. The union would make sense. Honda is a powerhouse in the U.S. market, while Mitsubishi is all over Asia. Their combined product line would range from Honda motorcycles to Mitsubishi trucks. Together, they would vault over Nissan Motor to become Japan's No. 2 auto maker, with combined fiscal 1995 sales of \$76 billion, vs. Toyota Motor's \$83 billion and Nissan's \$60 billion.

Predictions of a Honda-Mitsubishi marriage aren't new, but they were revived by the spring megamerger announcement of Bank of Tokyo and Mitsubishi Bank. Why? Mitsubishi Bank is the main bank for both companies and holds nearly 5% of

the shares in each, while Bank of Tokyo also owns a chunk of Honda. In Japan, banks traditionally play the role of matchmaker. Other circumstantial evidence: Honda has been asking analysts, such as James Capel's Matthew Ruddick, for their reports on Mitsubishi. And there's room at the top at Honda, as if there was some anticipation of big management shifts. Its chairmanship has been vacant for two years.

With 11 players, some consolidation is inevitable for Japan's auto industry. Mergers, unpopular in Japan, have nevertheless been rising of late, up 7% in 1995's first half, reports Daiwa Securities.

Skeptics note that mergers are usually last-ditch efforts of small, troubled companies. Honda and Mitsubishi are both healthy. Big corporate news is often spread in advance as rumor so everyone can adjust. For example, the bank merger was rumored for years before it actually happened. *Edith Hill Updike*



## TALK SHOW "Put in layman's terms, DuPont cheated"

—U.S. District Judge J. Robert Elliott, imposing a \$115 million fine for allegedly withholding data and fudging results in a pesticide lawsuit. DuPont denies this.



## AT IMMIGRATION The usual wa

cialists discover undocumented immigrant. Since revenue from has dropped to \$13.4 million year, as the ai screened pa

## BORDER PATROL

### ALIEN INVASION OR REVENUE GRAB?

AIRLINES, LATELY MORE diligent about keeping passport- and visa-less aliens from scamming their way into the country, aren't getting much credit from Congress. Many lawmakers want to raise the fine—from \$3,000 to \$5,000—that carriers pay each time Immigration & Naturalization Service offi-

gers more effectively. Genes William Noonan, an Transport Assn. spokesman. "They may be trying to the revenue back up."

Lawmakers say they to goad foreign airlines—as less watchful than ones—into cracking down all the dodges. A con ploy: A foreigner board plane using fake papers won't withstand Immigration scrutiny, ditches them b landing, and once on soil, demands political lum. *Christina Del Valle*

## FLOPPY FEVER

### A SUMMER BUG STINGS AMEX

OOPS. THIS WASN'T QUITE THE impression American Express wanted to make. A promo diskette, sent out to trumpet its new SmartData software, has a virus. A reporter who got the disk spotted the bug. The problem: Interactive Di-

rect, the company that created the demo disk, inadvertently transmitted a virus when it copied the prog. The actual SmartData program, produced internally for AmEx for its 401(k)-spe clients, wasn't corrupted.

Interactive President chael Bonner, in a mem taint-disk recipients, scribed a "nondestructive rus" that "does not go ou its own to destroy dat files." Even so, he ad there's a remote chance if a hard drive is filled to brim, the virus could interfere with its ability to member where all the are. AmEx quickly patched a "clean" replacement disk, along with McAfee Virus Detection ware. *Edward C. E*



## THE LIST SINKING SYNDICATIONS



VANNA: *Creaking Wheel*

Ted Turner wanted to buy syndicator King World because he figured its rich cash flow could help him bag CBS. Well, maybe it's a good thing his board scotched that plan. Investment bankers say King World, which boasts the top three syndicated TV shows, may be peaking. Reason: drooping ratings hurting all syndicators, due to competition from cable. Viewership for the top five shows this season is markedly down from that of the 1980s leaders.

### TOP SYNDICATED SHOWS

Average Weekly Viewership

| 1994-95 Show                 | Syndicator  | Households* | 1987-88 Show                 | Syndicator  | Households* |
|------------------------------|-------------|-------------|------------------------------|-------------|-------------|
| 1 WHEEL OF FORTUNE           | KING WORLD  | 12.2        | 1 WHEEL OF FORTUNE           | KING WORLD  | 15.5        |
| 2 JEOPARDY                   | KING WORLD  | 10.1        | 2 JEOPARDY                   | KING WORLD  | 12.5        |
| 3 OPRAH WINFREY              | KING WORLD  | 7.8         | 3 WORLD WRESTLING FEDERATION | TITANSports | 9.3         |
| 4 BUENA VISTA (DISNEY) MOVIE | BUENA VISTA | 7.2         | 4 UNIVERSAL PICTURES MOVIE   | MCA         | 8.9         |
| 5 ENTERTAINMENT TONIGHT      | RYSSER      | 7.0         | 5 STAR TREK                  | PARAMOUNT   | 8.8         |

\*In Millions

DATA: NIELSEN MEDIA RESEARCH

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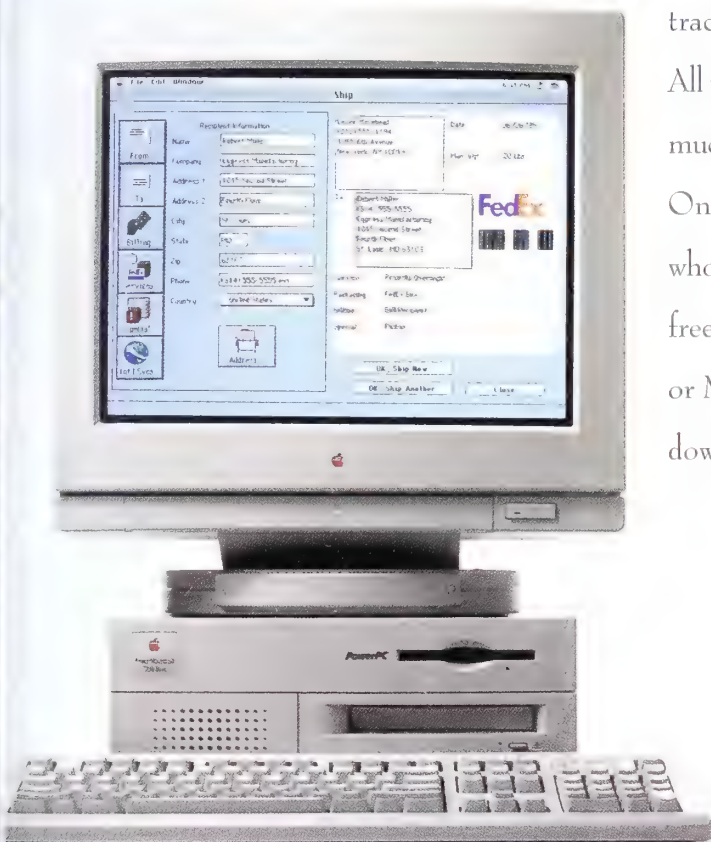
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## BANK NOTES

### PENNIES FROM HEAVEN—ER, ATMs



**BAIT:** Use a machine, please

TO BANKS, CUSTOMERS ARE about as welcome at teller windows as Bonnie and Clyde. It costs a bank twice as much to serve a typical customer at the window as it does at an ATM, say industry analysts. So some banks, to the vexation of depositors, are charging fees for seeing the teller. But one institution, Baltimore's 1st Mariner Bank, has just taken the opposite tack: paying folks to use an ATM.

## LOGOS

### HORNING IN ON A SEXUAL MYTH



EXXON HAS A tiger, Met Life has Snoopy, Disney has Mickey. But what's your corporate mascot if you're in the business of combating

impotence? Vivus, a pioneer in this growing field, has adopted the rhinoceros. The Menlo Park (Calif.) company unveiled the symbol in its recent annual report. Says Barbara Clark, Vivus' head of investor relations, a rhino with a zesty, upturned horn was chosen partly because he's "a pretty macho animal."

There's also an environmental angle. Rhinos are endangered because of a myth that their horns yield a powerful aphrodisiac and impotence remedy. Vivus' main

The small, six-branch bank, which opened just a year ago, pays customers a quarter each time they go to an ATM—up to \$1 per month. "We need to build our customer base," says CEO Edwin Hale. Since the program began only in July, it's too soon to tell if this has worked. But some larger banks are using ATM incentives, too. BankAmerica, for instance, just started reducing basic monthly checking fees from \$8 to \$4.50 for customers who do withdrawals and deposits on an ATM.

Trouble is, most big banks prefer the stick to the carrot. This spring, First Chicago irked a lot of customers when it implemented a \$3 charge on smallish account holders each time they make a withdrawal or deposit with a teller after four to six visits per month. Roy Furchgott

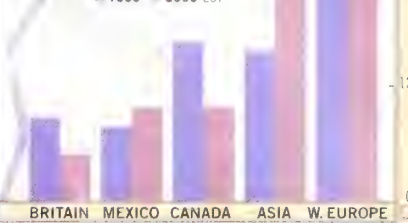
product, now undergoing clinical trials, is more prosaic: a special device that inserts a drug to produce an erection. Vivus' annual report deadpans that the company hopes this product will be so successful it will "help protect the rhinoceros from extinction." Joan O'C. Hamilton

## THE BIG PICTURE

### The Lure of the Orient

**BIG-COMPANY CEOs NAMING THEIR NO. 1 OVERSEAS MARKET IN PERCENT**

■ 1995 ■ 2000 EST



The shift is on from Europe to Asia as the focus for U.S. companies, according to a poll of CEOs of 1,000 big companies. NatWest Securities says the results suggest that oil companies such as Exxon and Mobil, which have extensive Far East operations, will be big winners.

DATA: DELOITTE & TOUCHE/WIRTHLIN GROUP

## DRAWN & QUARTERED



## UBER ALLES

### GERMAN BREWERIES ARE GOING FLAT

FOR GERMANY'S BREWERS, this isn't a time for merry-making. Traditionally, Germans flock to a *Biergarten* in the summer to hoist liter-size mugs and belt out drinking songs. Yet although Germans still savor more suds than anyone else but the Czechs, they are tipping back less than they used to, often reaching for mineral water instead. With nearly 30% overcapacity and half of the country's 1,278 breweries

in the red, analysts see a major shakeout looming. 600 to 700 will survive decade's end, predicts chael Dietzsch, president of the German Brewers Association. So brewers are forced to adopt new strategies, such as producing low-calorie



**OKTOBERFEST:** Fewer drinkers these days

nonalcoholic beers. In a country where no label has more than a 5% market share, some are pushing beyond regional niches. For instance, Bitburger, whose traditional pilsner is made in the area south of Bonn, is bidding for a wider following by sponsoring Formula One racing.

Others are hoping the German reputation for good beer will carry them into international markets. Now, only 1% of German beer is exported, with Beck's and Holsten accounting for 40% of the total. Although giants on the order of Heineken and Kaiser-Busch are entrenched in key locales around the world, German brewers are eyeing growing markets in eastern Europe and Asia. Karen Lowry M

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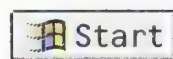


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## LET THE STATES DEAL WITH SPEED LIMITS

Your article "The cost of new speed limits" (Economic Trends, Aug. 14) states that our oil usage will increase with the increase in legal speed limits and has found an oil analyst to agree. Let me suggest that the author and the analyst take a ride on any nearby interstate highway and do a little research.

The writer is correct that fuel economy will decrease with an increase in speed. What he fails to state is that the majority of the trucks and autos are already at or above the speed limits being discussed in Washington. All the law will do is decrease the number of "law-breakers" already exceeding the current limits and decrease the all-too-plentiful opportunities for law enforcement to apprehend "speeders" who are merely keeping up with the flow of traffic.

What we need is to get Washington out of our lives and let the people deal with this issue on a state-by-state basis.

Thomas N. Tone  
 Simi Valley, Calif.

## THANKS FOR THE REMINDER OF PRU-BACHE'S GREED

It has been nine years since we partook of a Prudential-Bache Securities Inc. public seminar "to learn more about various safe income investments..." We have since learned the hard way, along with thousands of others.

Thanks for reviewing Kurt Eichenwald's *Serpent on the Rock* in "How greed poisoned Pru-Bache" (Books, Aug. 14). Too bad CEO George L. Ball and James J. Darr, who headed the firm's limited-partnership department, can't be required to buy copies of the book for every single library in the country.

A. O. McDonald  
 Boulder, Colo.

## THERE'S JUST ONE REASON WHY MIKE MILKEN PLEADED GUILTY

So, Mike Milken was innocent, suggests "Success was Mike Milken's real

## CORRECTIONS & CLARIFICATION

"The printer king invades home PCs" (Information Processing, Aug. 21) should have said that Hewlett-Packard Co. hopes to retain the No. 3 position in that market in 1997, not this year.

In "Ladders to help climb your family tree" (Personal Business, Aug. 14), the author of *Genealogy Online: Researching Your Roots* should have been identified as Elizabeth H. Crowe. The correct list price is \$27.95.

In "Times Square: From filth to fantasy" (Letter From New York, Aug. 21), which appeared in some editions of BUSINESS WEEK, the location of the New Amsterdam Theater should have been 42nd Street, not 41st Street.

crime" (Economic Viewpoint, Aug. 14), Paul Craig Roberts maintains that "copping a plea," Milken cast himself in the role of a guilty party. Let me suggest a simpler explanation: In Milken's plea, he pleaded guilty to six felony counts because he was in fact... guilty. To claim that an innocent man, the finest legal counsel, pleaded guilty to crimes he did not commit because the media hounded him even though he was aware that such a plea would guarantee prison time is an absurdity.

Joe Ben  
 Summit, N.J.

## PROTECT INVESTORS—BUT DON'T PENALIZE CEOs

With interest and approval I read "A better way to protect investors" (Editorials, Aug. 14). However, I agree with your advocacy of the measures we have known or should have known about. This is like Monday morning quarterbacking about the competence or lack of clairvoyance of a CEO. To have a CEO into court for fraud is disingenuous.

John G. A.  
 Chairman  
 Adaj  
 Milpitas, Calif.

## Business Week

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## PRICE ISN'T JOB ONE COMPUTER SUPERSTORES

I appreciated your writer's comments about the lack of decent service at computer superstores in "Tips for the shop-weary" (Technology & Aug. 14). I admit I've been seething by the selection at CompUSA and going back, even though I've been led by their lack of knowledgeable people. Once, I waited 20 minutes for the "only guy in the store who's about faxes." By the time he showed up, I had read all the products and had narrowed my choice to two models. I only wanted to know the difference between them. He looked at me blankly and then started reading the faxes! I should have walked out, but I bought one anyway. I guess as long as we keep buying, they'll keep growing. Small, independent stores need to do a better job of serving our needs. Price is not always the first priority.

Erin Palmeter  
San Diego

## CHRISTIAN FICTION A REAL KICK

I was disturbed by your characterization of Christian fiction ("Onward, Christian publishers," News: Analysis & Commentary, July 31) as having stale plotlines." Apparently you read none of the work of Brock Bodie Thoene, who are listed in your article. Granted, there is no illicit sex, but there is enough murder, deception, intrigue, and suspicion to rival any secular author.

Kimberley M. Jensen  
Dalton, Ga.

## TO REACH BUSINESS WEEK

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## ADVICE & DISSENT

They're The McLaughlin Group. Each with a view that's contentious and contagious. (clockwise from left) Jack Germond, Clarence Page, John McLaughlin, Eleanor Clift, Morton Kondracke and Fred Barnes.

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**WHEN THE PENTAGON WAS FOR SALE**  
**Inside America's Biggest Defense Scandal**

By Andy Pasztor  
 Scribner • 416pp • \$25

# ARMING THE NATION— AND PICKING YOUR POCKET

**J**ohn Marlowe's sex drive kicked into high gear the instant he spotted the two little girls."

With this grabber, Andy Pasztor begins his disturbing tale of defense fraud, 1980s-style, *When the Pentagon Was for Sale*. According to Pasztor, Marlowe was one of dozens of Reagan Administration-era defense consultants who took the term Beltway Bandit literally. A six-year sentence for child molestation was hanging over him when the government got a tip that he had solicited a bribe from a defense contractor. Under pressure, Marlowe agreed to become an undercover informant for prosecutors who were just beginning to investigate a defense-corruption scandal that would make Teapot Dome look like a minor tempest. A tap on Marlowe's phone led to other culprits and a total of 76,000 intercepted conversations. Federal agents overheard candid discussions of payoffs large and small and of successful efforts to steer Pentagon contracts to favored companies.

Two federal investigations, dubbed Operation Illwind and Operation Uncover, proved that such fraud was no aberration. More than 90 individuals and companies, including 8 of the 15 largest Pentagon suppliers, were ultimately convicted of or pleaded guilty to charges ranging from bribery to illegally obtaining competitors' cost data. The roster included General Electric Co., Boeing Co., former Assistant Navy Secretary Melvin Paisley, and a host of consultants who traded on friendships to rake in hundreds of thousands of dollars for themselves and billions for their corporate clients. (For his cooperation, Marlowe, on the other hand, was never charged

with soliciting a bribe, and the government paid some of his bills while he was in prison for the sex crimes.)

Many of these consultants, it turned out, knew nothing about weapons technology: As his friends were wont to joke, one consultant's definition of a universal joint was "a really big nightclub open to everyone." And much of what they and the contractors got the government to purchase, such as \$116 million worth of shipboard radar-upgrade kits, was either unnecessary, obsolete, or overpriced.

Pasztor, who covered the scandal for *The Wall Street Journal*, shows how the Reagan Administration's lack of ethical awareness and its market-oriented reform efforts contributed to the land-rush climate. Unfettered by ethical rules, Reagan's Pentagon transition-team members had ready access to some of the Defense Dept.'s innermost secrets—which some of them employed for private gain. One top transition official

was Benjamin T. Plymale, a senior executive at Boeing, whose colleagues, Pasztor says, photocopied a treasure trove of Pentagon documents from the transition team's safe.

Even well-intentioned efforts to reform procurement backfired. In the midst of a fleet buildup, Navy Secretary John F. Lehman vastly increased the number of contracts open to competitive bids. He shifted from the practice of providing cost-plus deals—thought to encourage wasteful practices—to fixed-cost contracts. And Lehman sometimes had two companies make the same weapon. These moves were intended to drive prices down and to shift the risk of cost overruns to suppliers.

But Lehman, as arrogant as underlings who never thought they would get caught, refused to acknowledge these efforts weren't working. The real rivalry turned out to be not in pricing but for inside information on coming procurements and over generous specifications tailored to a company's advantage. Making matters worse, the lead contractor was allowed to be the second source for manufacture of a weapon. As William Galvin, one of the consultants at the heart of the investigation, explained to a grand jury, they then avoid aggressive competition. "You pick a friendly, docile second source," he said. "You don't pick a tiger."

Pasztor paints detailed portraits of some of these central figures. At times this approach slows down his account, but once the author turns to the investigations, the book picks up speed. While the probes were unfolding, Marlowe didn't have the public impact of the savings-and-loan debacle or other scandals of the 1980s. So *When the Pentagon Was for Sale* serves as an important reminder of why government officials and procurement must undergo enough scrutiny.

Have the seeds now been sown for a replay of the skulduggery, Pasztor wonders? With procurement budgets falling at about half of their 1987 high, constant dollars and with the defense industry suffering through a wrenching retrenchment, pressure for inside information and help winning contracts is greater than ever. What's more, Pasztor points out, some of the more rigorous requirements have been eased.

Whether or not he's right, the scandal's legacy will continue to dog the Pentagon. In an added wrinkle, tight budgets are pushing the Pentagon to seek cheaper nonmilitary products, from computers to nails. But, like defense contractors, commercial vendors gripe about procurement rules, and they may be unwilling to do business with the Pentagon unless the rules are abandoned. It's a dilemma that policymakers are only beginning to face. Given competitive pressures and the dusty clout that Pasztor details, it's difficult to believe that the problem will be solved wisely.

BY STAN CR

*Crock covers national-security affairs for BUSINESS WEEK.*



## SKULDUGGERY DURING THE REAGAN-ERA DEFENSE BUILDUP LED TO BILLIONS IN RAKE-OFFS

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- 3 THE BEARDSTOWN LADIES' COMMON-SENSE INVESTMENT GUIDE** by the Beardstown Ladies Investment Club with Leslie Whitaker (Hyperion • \$19.95) *Recipes for Four-Bean Salad, Five-Hour Stew—and 23% returns.*
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- 12 THE HP WAY** by David Packard (HarperBusiness • \$17) *Hewlett-Packard's co-founder tells how the giant grew from its humble origins in a Palo Alto garage.*
- 13 RAVING FANS** by Kenneth Blanchard PhD and Sheldon Bowles (Morrow • \$20) *How to turn customers into your biggest boosters.*
- 14 WHY GOOD GIRLS DON'T GET AHEAD... BUT GUTSY GIRLS DO** by Kate White (Warner • \$21.95) *Career strategies from a former goody two-shoes who got wise.*
- 15 HOW TO DRIVE YOUR COMPETITION CRAZY** by Guy Kawasaki (Hyperion • \$22.95) *Pulling off the gloves—and giving the other guy fits.*

## PAPERBACK BUSINESS BOOKS

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- 2 THE 1995 WHAT COLOR IS YOUR PARACHUTE?** by Richard Nelson Bolles (Ten Speed Press • \$14.95) *The enduring job-search bible.*
- 3 THE WALL STREET JOURNAL GUIDE TO UNDERSTANDING MONEY AND INVESTING** by Kenneth M. Morris and Alan Siegel ( Fireside • \$13.95) *Concise explanations enriched with graphics.*
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BUSINESS WEEK's Best-Seller List is based on a survey of chain and independent booksellers that carry a broad selection of books on economic management, sales and marketing, small business, investing, personal finance, and careers. Well over 1,000 retail outlets nationwide are represented. Current rankings are based on a weighted analysis of unit sales in July.

## TO OUR READERS

We are changing our Best-Seller List. Ever since such lists were invented, authors and publishers have tried to figure out how they could be manipulated. So we built safeguards into our data-collection to thwart tampering. In recent months though, as news stories in this magazine have shown, there have been several successful attempts to maneuver books onto best-seller lists.

The BUSINESS WEEK stories reported

that, early this year, authors of *The Discipline of Market Leaders* bought more than 10,000 copies of their own book from bookstores thought to submit data to *The New York Times*. At about the same time, another author, James Champy, purchased 7,500 copies of his *Reengineering Management* from bookstores. In each case, the books landed on best-seller lists. The potential rewards: credibility, speaking engagements, and consultancy work.

To avoid such manipulation, we will,

as of this month's list, no longer publish the names of the reporting bookstores. Also, BUSINESS WEEK will add several stores to those that currently report monthly sales. Each bookstore will be asked to filter out corporate sales that seem designed to influence a book's standing on our list. Each month, we will calculate the results using a different subset of reporting stores, to reduce the chance of manipulation further. And we'll be even more diligent about checking our numbers.

# IT-WORLD NEWS



## Dallas/Fort Worth: Pyramid provides big lift at Dallas/Fort Worth International Airport.

Running the world's second largest airport up and running is no small feat. Each year, more than 52 million passengers travel through Dallas/Fort Worth International Airport on their way to destinations around the country and around the world.

Managing traffic and the development of more sophisticated, time-sensitive applications prompted the airport's Systems Technology Management organization to begin looking for a very high-performance enterprise-class solution that could enhance the existing technology offering without

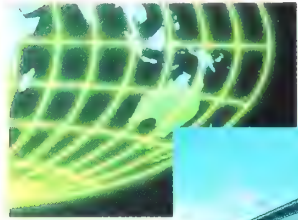
creating a disturbance in day-to-day operations. The solution? Pyramid's high-performance, high-reliability Nile 150 symmetric multiprocessing server. Based on the MIPS R4400 architecture, the Nile provides unprecedented levels of reliability, availability, and serviceability. Teaming with strategic partner ORACLE Corp., Pyramid provided Dallas/Fort Worth International with a complete systems solution, including the extremely high-performance enterprise-class Nile 150 server as well as ORACLE's relational database management system and a comprehensive package of business applications

such as financial management, order processing, personnel, purchasing, inventory control and traffic analysis.

The impact of the Pyramid solution has been excellent. The more than 700 airport employees who rely on the Nile to keep the airport up and running report excellent response time and performance from the system, and airport management is now able to rely on a fuller range of programs to manage the onslaught of traffic at one of the world's busiest travel hubs.



## Melbourne: Pyramid is on top "down under".



AV Jennings, the largest home building contractor in Australia, is counting on Pyramid Technology to give it the advantage it needs to better compete in the country's slow housing market. With a Pyramid Nile 100 server now installed at its headquarters site

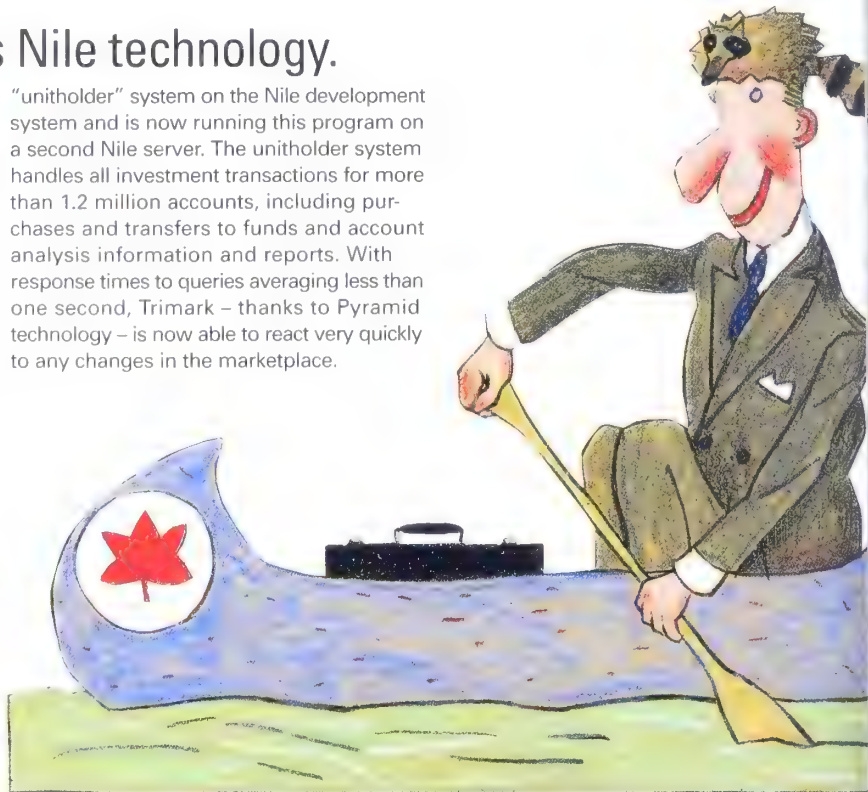
in Melbourne, AV Jennings gets the speed, accessibility and aggressive price/performance it needs to stay competitive. According to Andrew Piddington, AV Jennings' Computer Services Manager, the company invited several vendors to perform benchmark tests to help it determine the best vendor for the job. "The Nile system outperformed the others," says Piddington. The Australian company discovered that the Nile 100 was capable of delivering all the performance, reliability and availability of a high-end server at only a fraction of the cost. From AV Jennings' perspective, the fast response times that the Nile provides to queries enables the company to process and deliver information in a far more timely and efficient manner.

In addition, the Mirror Disc capability provides maximum security. The Nile 100 server supports a network of nearly 200 offices with vital information generated by ORACLE and other sector-specific software vendors. The software, specifically targeted to AV Jennings' business, provides the "bill of quantities" for all house designs, calculates pricing information and issues purchase orders for all jobs. "The new system has made a dramatic improvement in response time and has reduced our costs," explains Piddington. With the Nile 100 server, AV Jennings has an open UNIX<sup>®</sup> platform that gives the company access to a wider range of software solutions, making it easier to integrate their resources – thereby protecting their hardware and software investments as they grow. With Pyramid's flexibility and performance, the Nile system will remain "on top down under" for years to come.

## Toronto: Trimark trusts Nile technology.

More than 800,000 Canadians have entrusted more than 12 billion in investments to Trimark, one of Canada's leading mutual fund management companies. With this sizable fund to manage, Trimark needed a technology solution that it could trust as well – one that would provide superb functionality, unmatched scalability and excellent price/performance. It turned to the Pyramid Nile 150. Trimark installed three Nile servers at its headquarters office in Toronto for marketing, software development and business data output. ORACLE teamed with Pyramid to provide some of Trimark's business applications at this site. The Pyramid UNIX servers have been integrated into a local area network (LAN) of over 300 workstations. Via Trimark's wide area network (WAN) access is also provided to over 300 financial planners. With the Nile 150s, Trimark's employees are better able to access and analyze enormous quantities of data quickly and more efficiently. While all processing takes place on-line, vast amounts of data are simultaneously batch-processed and backed up. For example, Trimark programmed the

"unitholder" system on the Nile development system and is now running this program on a second Nile server. The unitholder system handles all investment transactions for more than 1.2 million accounts, including purchases and transfers to funds and account analysis information and reports. With response times to queries averaging less than one second, Trimark – thanks to Pyramid technology – is now able to react very quickly to any changes in the marketplace.



## Stockport/Cheshire: adidas gets fit with RM600.

adidas (U.K.) Limited, Britain's leading sports goods manufacturer, broke all records with the speed of its conversion from a mainframe to the latest client-server architecture. With the assistance of Siemens Nixdorf, adidas' Department installed an RM600 UNIX server over just one weekend and the entire IT organization changed their systems over to distributed information processing. Handling all the queries from over 200 PC users connected to the system is just a short sprint for the high-performance computer. Comprehensive management reports previously taking hours to produce are now available in minutes, information which took minutes to produce is now available in seconds. This is just one benefit adidas gets from RM600 – the sheer power of the system providing extremely rapid response times to the entire network. "The migration was



potentially a high risk operation but was accomplished successfully, on time and with the least possible disruption", says Paul Farrington, Operations Manager at adidas. The dramatic time-saving achieved with the RM600 enables adidas to respond to their customers' needs more efficiently, and provides detailed sales and marketing data aimed to keep adidas at the leading edge of the British sports goods trade.

## Cologne: For Gerling, there's no parallel to the Reliant RM1000 parallel computer.

The world's first order for a Siemens Nixdorf Reliant RM1000 isn't Gerling's first order for an RM System: Gerling, one of Europe's largest insurance companies, has been depend-

ing on UNIX servers for years to run a multitude of applications in a wide range of sectors.

The insurance company currently uses some 4,000 desktop terminals and approximately 2,200 PCs. With the Reliant RM1000, Gerling is adding the newest and most innovative product from the UNIX RM system family.

What's new about the Reliant RM1000 is its massively parallel architecture. Together with the R/3\* business software

suite from SAP, it will afford Gerling a significant increase in performance to support the company's decision-making processes.

The 18 processors in the Reliant RM1000 will assure ultra-fast management of all tasks. Within a fraction of a second, it will process enormous volumes of data from the R/3 cost and financial management modules, store comprehensive information in the Compact optical archiving system, or route it right to the workplaces.

An R/3 production application with 300 users will run on the Reliant RM1000. At the same time, though, it will still provide ample performance reserves for programming and testing new or additional R/3 applications – all of them in parallel on one system.





## Paris: RM computers help SNCF set the course for UNIX.



SNCF, the French railway company has, together with Siemens Nixdorf, already set the course for a state-of-the-art payroll system. Here's the background. For greater efficiency and lower costs, SNCF has recently rationalized its train and service personnel into fewer locations. More than 50 RM200 and RM400 systems have been installed to collect data on the hours worked by the train crews: train drivers and service staff for the rolling stock. The UNIX systems have been installed nationwide in the equipment and locomotive departments and are part of a project aimed at making the calculation of salaries more efficient. Siemens Nixdorf managed the entire

migration project, from the proprietary system to UNIX. The principal job of the RM computers is to keep an exact account of the wide differing hours worked by the SNCF train crews, monitoring night rates and weekend work, for example. Seamlessly integrated into the existing communications network, the computers feed the data via SNCF's private data network through to the payroll system at headquarters. With this, SNCF employees can rely on an impeccable payroll system even after the reorganization. At SNCF's headquarters always have an overview of the costs and productivity rate of 16,000 people employed in the train crew.

## From RM200 to BS2000/OSD: Integrating power for open, enterprise-wide computing.

Open, enterprise-wide computing is putting new power into modern client-server networks. Massively parallel architectures provide a quantum leap in performance, availability and flexibility. Now, for example, the huge volumes of data in large organizations can be utilized to enhance decision-support processes. Precision marketing is now a reality. Siemens Nixdorf offers a spectrum of hardware power for open, enterprise-wide computing that's unrivalled by other computer vendors: the world's largest line of

computers, from desktop systems to high-performance servers – with the operating systems our customers need most: UNIX, NT and BS2000/OSD.

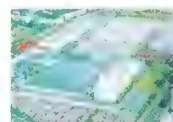
With RM200, RM400 and RM600, Europe's successful multi-user UNIX systems. With BS2000/OSD, the general purpose mainframes that offer the openness to interoperate with both UNIX and PC systems. And now, with the first jointly marketed high-end server from Siemens Nixdorf and Pyramid Technology: the Reliant RM1000. Its more than 10 tera-

bytes of on-line information make it the powerhouse among parallel servers. The Reliant RM1000 can be upgraded to incorporate hundreds of processors – for processing massive volumes of data in both traditional and open environments. And for high-end performance in handling complex R/3 applications and leading-edge solutions like data warehousing, decision support or video server applications. Unlimited computing power for your open enterprise-wide computing needs.

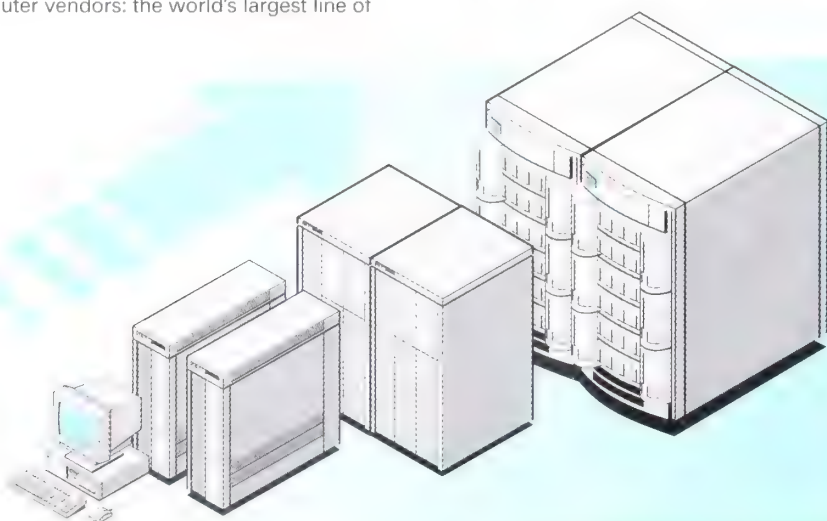
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STEPHEN H. WILDSTROM

## YOU'LL LOVE THIS NETWORK BATTLE

Those of us in the vicinity of Washington, D.C., were more than a little worried a couple of weeks back as Hurricane Felix threatened the Middle Atlantic coast. So I got some sense out of comfort by clicking an icon on my computer screen every now and then to effortlessly get the latest news from the National Weather Service as I went about my work. Such quick and easy access to information on demand got me to thinking about networking, the next frontier in computer services for companies and individuals. And what I see is a battle shaping up in the software industry, an indication that we are likely to see dramatic improvements in computer networking very soon.

The promise of network services is great. There is far too much power in today's personal computers to stay locked up in a box on our desktops. We need software that lets us reach out to collaborate with co-workers, gives us instant access to information around the world, that allows us to manage such mundane tasks as rolling the air-conditioning and security systems in homes.

**THE DEFINITION.** The networks of the not-very-distant future will provide an instantaneous transfer of information, and the computer will finally fade into the background as a tool. The distinction between data on your computer and data on the network will disappear. "The notion of networks is arising from connecting

computers to connecting people," says Novell Inc. Chief Executive Robert J. Frankenberg. "It's a time of great promise and great peril" for the industry.

The situation is in sharp contrast with the history of the computer operating system, where the evolution



from clunky DOS commands to Microsoft's Windows 95 was painfully slow. Microsoft, which was handed a virtual monopoly in PC operating systems by IBM 14 years ago, is starting out well behind in the networking race. Novell has far greater network experience and better software. IBM and AT&T have deep pockets and a lot more networking expertise than Microsoft. And a batch of aggressive new competitors, including telephone and cable television companies, want a piece of the action.

The E-mail and group-

ware we see in companies and the online networks we peruse at home are just a glimpse of what the next generation of connectivity will bring. If you've had the good fortune to work on a system with a fast, direct connection to the Internet, you will understand just how different the experience of instant access is from fetching information using a dial-up service. A high-speed connection helped my watch on Hurricane Felix seem effortless as I sat at my desk. But because I helped design and install the system that made it possible, I knew first-hand about the immense software

framework needed to make it work.

Sooner rather than later, such connections will become cheap and available for homes and small businesses. The prerequisite will be digital telephone lines or cable television circuits. But software will have to make the setup vastly easier for people who don't have network administrators.

The uses for the networks will be limited only by imagination. Novell, moving in where Microsoft has already flopped, hopes to extend the network to all sorts of de-

vices. Novell Embedded Systems Technology (NEST) would allow you to find the copier with the shortest wait or check to see if a fax has come in. At home, your heating and cooling system, your security system, even your VCR, would be tied into a network, probably using the existing electrical wiring, and would be controlled by your computer.

Microsoft dreamed of similar networks with its "Windows everywhere" strategy. However, Microsoft At Work, a system for controlling fax machines, copiers, and other office equipment failed dismally because no one wanted to add the hundreds of dollars worth of electronics to enable a fax machine to run the software. The NEST program, by contrast, can be embedded in an inexpensive handful of chips.

**TEDIOUS PROCESS.** Microsoft knows the future is in networks. An icon called Network Neighborhood is a basic feature of the Windows 95 desktop. The Help menu in Microsoft Works 4.0 includes an item that will automatically dial up the new Microsoft Network (MSN). There you can look for assistance from tech support or other users of the integrated word processor/spreadsheet program. Good idea. But you have to twiddle your thumbs while your modem churns away. And once you get online, you fight your way through a series of screens, each seeming to take minutes to appear. All in all, a frustrating process.

Despite its poor position in networking, I would hardly bet the ranch against the giant of Redmond, a smart and fierce player at the top of its game. However, in the end, it matters little who wins the next round of the software wars if the competition brings rapid progress. And for this, the prospects are bright.



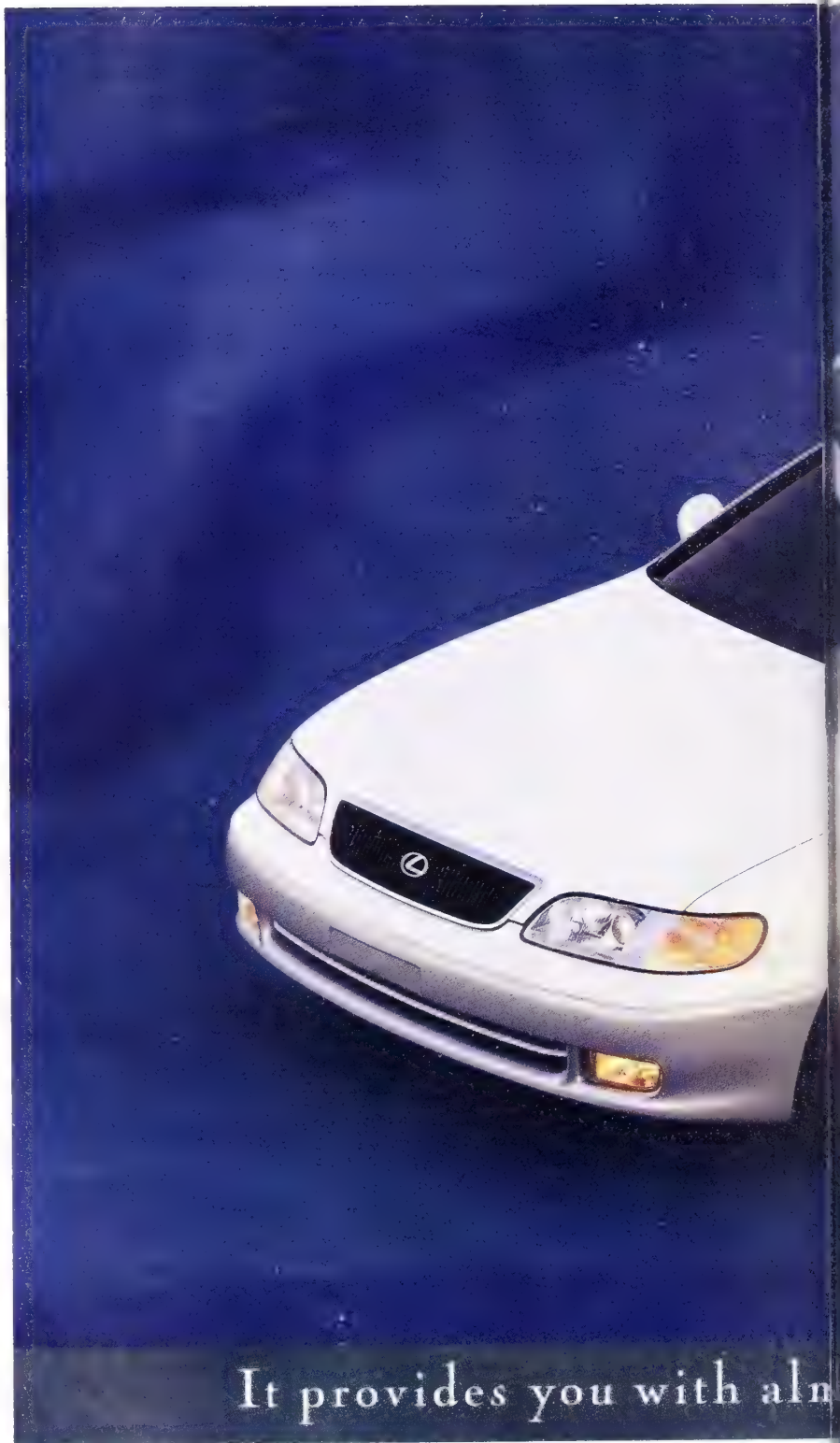
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BY ROBERT KUTTNER

## THE NET AS FREE-MARKET UTOPIA? THINK AGAIN



### HYBRID:

The Internet is sure to become a commercial hot spot. But it sprang from the government—and users are committed to free information

Many prophets of cyberspace think the Internet is the apotheosis of the marketplace. The whole affair is marvelously decentralized and self-executing, with no need for pesky regulations. Any seller can offer wares to any buyer, worldwide. For theorists such as authors George Gilder and John Naisbitt, and for Peter Huber of the Manhattan Institute for Policy Research, the world of computer-mediated communication realizes a market utopia—Adam Smith with a computer.

I'm not so sure. For starters, consider the history of the Internet. It grew out of the Defense Dept.'s Advanced Research Projects Agency Network (ARPANET), a system designed to link remote computers for purposes of weapons development, military command and control, and pure research. The government funded most of the early advances that made possible today's user-friendly home computers linked by phone lines—packet switching of data, graphical interfaces, and the architecture of the Net itself.

Where the Pentagon left off, the university and scientific community picked up. The forerunners of the Internet, such as BITNET (a nonprofit inter-university cooperative) and the National Science Foundation's NSFNET, were developed mainly for research purposes. Usage was subsidized by government. Although some private companies, such as Xerox Corp. (through its Palo Alto Research Center, PARC), contributed to the technology underlying today's Internet, nobody imagined that a network designed for defense communications would someday be used for home shopping.

**RIDICULE.** When the linkage of remote computers was still in its infancy, the prospect of commercial payoff was so distant and improbable that no private company could have justified the venture based on the profit motive. Although the AT&Ts and IBMs of that era had plenty of scientists and deep pockets, the Internet was spawned not by private investments but by the Pentagon and the universities—the two principal centers of technical virtuosity with goals other than profit.

Moreover, as the Internet developed, so did a unique subculture—one intensely committed to decentralization and open access but also skeptical of opportunism and profiteering. Early attempts to use the Net to advertise were roundly “flamed”—bombarded with scorn and ridicule—by Net aficionados.

The guardians of Net culture and the brants of cybercapitalism share a reverence for benign anarchy but not the same ship of the profit motive.

Surfing the Net, one appreciates that of the thousands of “Web sites” offering information to anyone who logs on are free sites—typically put online by enthusiasts for the sheer joy of discovery, invention, communication. Perhaps cyberculture's fiercely held tenet is that information ought to stay free.

Of course, the Internet is in its infancy as a commercial marketplace. Until now, it has been mainly a medium of scientific and search exchange, of chat groups for cancer patients, O.J. Simpson watchers, and thousands of other “virtual communities.” As social software is perfected assuring the security of credit-card purchases, amateur and profit uses will coexist uneasily with home shopping, pay-per-use entertainment, and other commercial ventures.

**PIGGYBACKING.** But the Internet will realize something other than pure capitalism. It would not exist if not for a scientific search, and hacker community with other market motives. While it is surely becoming a prime avenue for commerce, that is not its ethic. The ethic of free information is so deeply rooted on the Net that it's hard to see how fee-for-service data will drive out free data.

Some lessons here: Subcultures, contrary to both Karl Marx and George Gilder, are not mechanical reflections of material interests. They have a way of taking on lives of their own. Much of Internet culture is a distinctive hybrid, with as much in common with John Garcia as with Adam Smith. The conservative enthusiasts of technology and free markets, notably House Speaker Newt Gingrich, should think twice before they defund public scientific and technical research and turn the whole shooting match over to private enterprise. While the Net may be mostly self-governing, it's comforting to have the Justice Dept. in the background making sure that no single company takes over its gateways.

Entrepreneurs can surely piggyback on this remarkable infrastructure, profit from it, and carry it to the next stage. But they should realize whose shoulders they are standing on. And they may run into more resistance and a more complex set of values than they anticipate.

Robert Kuttner is co-editor of *The American Prospect* and author of *The End of Laissez-Faire*.

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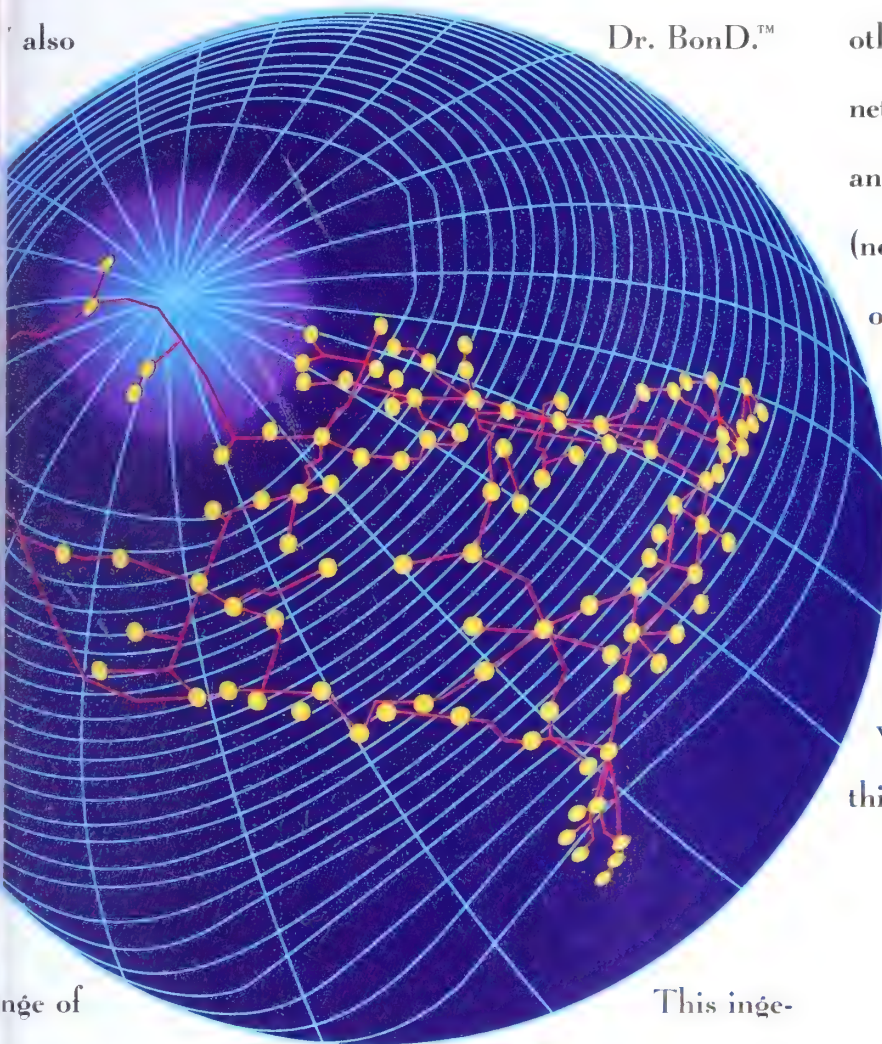
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BY GENE KORETZ

## IS A SHEEPSKIN WORTH IT ALL?

College education is under a cloud

Many parents of recent college graduates are frustrated these days. Despite the vaunted value of college, a lot of grads are taking low-wage jobs that require only high-school skills. Such experiences and recent reports that more and more U.S. graduates are employed in low-skill jobs raise troubling questions about the efficacy of investing in college.

A new study by John Tyler and Richard J. Murnane of Harvard University's Graduate School of Education and Frank Levy of Massachusetts Institute of Technology allays these fears. It finds that the low pay levels of many new grads only last for a few years (chart). Apparently, young graduates often take low-paying jobs temporarily, while

the 1980s," says Harvard's Murnane.

One reason young grads did better is that they responded to market signals by seeking degrees in fields with high and rising wages. Meanwhile, the real pay of less-educated workers was dropping sharply, and many older males found themselves with outmoded skills at a time of rapid technological change.

All of this underscores the value of a college education in today's turbulent labor market. Indeed, after rising modestly during the 1980s, the real median earnings of young male graduates actually dropped 4.4% from 1989 to 1993. In the same four years, however, the real earnings of young male high-school grads plunged 13.7%.

## YANKEES: NOSE TO THE GRINDSTONE

Their vacations are brutally short

Compared with counterparts overseas, U.S. employees get skimpy vacations. According to Hewitt Associates, a benefits consulting firm, American workers, after one year of service, average just two weeks of annual vacation. Same goes for Canadians and the Japanese—10 working days. In most European countries, by contrast, the mandated rule is 20 to 25 days (chart).

At big U.S. companies, Hewitt notes, employees usually fare better as their job tenure increases: three weeks of vacation after 5 years and four weeks after 15 years. But since many Americans work for smaller companies or often change jobs, in many cases they don't advance much past two weeks.

Runzheimer International reports that the average U.S. worker gets a grand total of only 17 days off a year, including holidays. By contrast, Swedes and Finns get 38 and 45 days, respectively. And with 21 national holidays, the average Japanese worker gets 37 days off.

## IMPORT TABS HIT A DOWNDRAFT

A stronger buck may ease price

The dollar's recent upsurge prompts hopes to lower the temperature in one of the few areas where inflation had been heating up this year: prices of U.S. imports, which account for around 30% of domestic demand for goods.

Economist Maury N. Harris of Price Waterhouse Coopers Inc. notes that import prices surged at an 8.2% annual rate in the first five months of this year, contrasting with an acceleration in consumer prices in the first half. And a big factor in the surge, he observes, was a drop of nearly 7% in the dollar's value against the currencies of America's 20 leading trading partners.

In June, however, import prices actually fell for the first time in nearly a year—with every product and region registering a decline. And with the dollar up appreciably since then, the slowing pace of import inflation seems likely to continue.

## BAD MARKS FOR PAY-BY-RESULTS

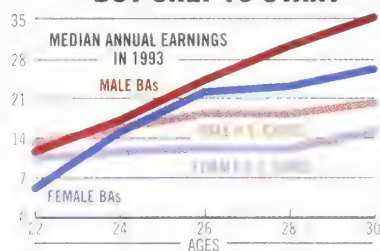
Teacher cash incentives don't work

It seemed like a promising idea: rewarding teachers with more pay for their students' performance improvement. But according to a recent Urban Institute study, it looks better on paper than in the classroom. In an analysis of 13 merit-pay incentive plans implemented by school districts around the U.S. in the 1980s and 1990s, the institute's researchers found that 11 had been terminated by 1993.

Most school districts trying merit pay plans did report some positive effects, such as declines in teacher absenteeism, improved teacher motivation and increased attention to teaching. But these were often offset by more problems stemming from increased rivalry among teachers and resentment when teachers were denied rewards they felt they deserved. High program costs and heavy demands on administrators also eroded community support for the plans.

The bottom line is that despite hopes, none of the 13 districts studied was able to use teacher pay incentives to achieve significant, lasting gains in student performance.

### COLLEGE GRADS: LOW PAY —BUT ONLY TO START



▲ THOUSANDS OF DOLLARS  
DATA: JOHN TYLER, RICHARD J. MURNANE, FRANK LEVY

searching for better opportunities. By the time they reach 30, most have managed to enter middle-class ranks.

As for rising "underemployment"—working in a job beneath your skill level—the study finds that this problem has afflicted primarily older men. During the 1980s, median real earnings increased among young (25 to 34) graduates of both sexes and among older (45 to 54) women grads—by 23% among younger and older women but by a modest 3% among the young men. And the share of underemployed workers in these three groups declined.

College-educated older men, on the other hand, lost ground. The share of 45- to 54-year-olds with BAS who had lower-skill jobs rose from 14.5% to nearly 18%, and their median real earnings fell by nearly 4%. "Older male college graduates were the chief victims of the wave of restructuring that surfaced in

### VACATION TIMES AROUND THE GLOBE

WORKING DAYS OFF  
ANNUAL VACATION ALLOWANCES\*



\* WITH ONE YEAR OF SERVICE  
DATA: HEWITT ASSOCIATES



AMES C. COOPER & KATHLEEN MADIGAN

## WHAT'S SABOTAGING GROWTH? THE STUBBORN TRADE GAP

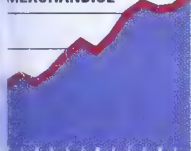
### U.S. ECONOMY

True or false: A weaker dollar, increased American competitiveness, continued recovery in Europe, and sharply higher U.S. growth have narrowed the huge American deficit. If you said true, join the throng. Many analysts thought the trade gap would be shrinking by now. Instead, foreign trade remains a big drag on the economy, and any significant relief may not be on the horizon until 1996—or later.

In June, the trade deficit for goods and services increased to \$11.3 billion, from \$11 billion in May. For goods alone, the gap was a towering \$16.4 billion, up from \$16.1 billion. Even after adjusting for prices, the deficit in goods continues to widen (chart).

### THE TRADE GAP IS STILL BALLOONING

#### MERCHANDISE



SOURCE: U.S. COMMERCE DEPT., LABOR DEPT., BUREAU OF ECONOMIC ANALYSIS

and GDP revisions are due on Aug. 30.

Exports are not the problem. The trouble is America's ever-growing appetite for imports. Goods exports have risen at an average 12.2% yearly pace for the past four quarters. The problem is that imports have been growing at a 13.4% clip for six quarters.

Stubbornly strong import growth means that, while U.S. manufacturers will continue to reap benefits from their increased competitiveness in growing foreign markets, others will get slammed by increased competition from abroad. That means gains in industrial output in the second half will be smaller than might otherwise occur in an economy expected to grow at an annual rate of 2% to 2½%.

### IMPORT DELUGE

has defied the restraints of a weak dollar and subpar growth. Why? Because no amount of productivity growth or dollar weakness can overcome the wage advantage of making sneakers in Asia or TVs in Korea, rather than in the U.S.

In June, imports of goods and services fell 0.6%, but followed a 1.2% gain in May. In the second quarter, imports grew at a 9.4% annual rate, little changed from their 10.1% pace in the first quarter and from

11.4% in the fourth. That's despite the sharply slower growth of total domestic demand—at an annual rate of 1% last quarter, down from 3.5% in the first quarter.

Foreign-made goods already capture a record 28.1% of nonoil goods purchases, up from 20.1% at the start of this expansion (chart). And it isn't just apparel and cars. Other imports, from semiconductors to railcars, are increasing as well.

Indeed, because of the strong yen and mark, the market share of imported cars in the U.S. has dropped considerably since the late 1980s. In July, foreign cars accounted for 20.2% of all cars sold, down from 30% in 1988. Add in light trucks and vans, which are mostly made stateside, and imports' share of motor-vehicle sales drops even more.

But other goods imports are soaring. So far this year, imports of nonauto consumer goods are up 13.9% from a year ago. Industrial supplies have jumped 19.8%. And capital goods have soared 21.6%.

In particular, the U.S. capital-spending boom has increased imports of advanced-technology products by 26.7% in the first half. Semiconductors are up 46.5%. U.S. exports of high-tech goods have increased by a much smaller 11.3%, causing a 36% decline in the trade surplus for advanced technology products.

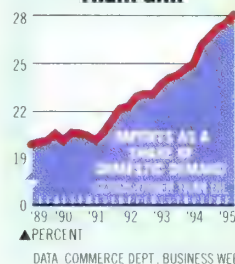
Since the U.S. addiction to imports seems impervious to anything but a recession, it is unlikely that import growth will slow by much in the second half. That means exports will have to shoulder most of the weight of reducing the trade gap.

### HAPPILY, THE EXPORT NEWS

is encouraging. Export growth has held up surprisingly well. Although overseas shipments of goods and services fell 1.2% in June, they are up 10% from a year ago. And that solid growth comes despite the economic troubles of America's three biggest trading partners.

Japan and Canada are struggling to post any kind of growth. Mexico is reeling from its steep peso devaluation in December and subsequent austerity measures in March (page 30). After seasonal adjustment by BUSINESS WEEK, Mexico's real GDP plunged at a 25% annual rate from the first quarter to the second, following a 10% drop from the fourth quarter to the first. Mexico's

### IMPORTS TIGHTEN THEIR GRIP



DATA: U.S. COMMERCE DEPT., BUSINESS WEEK



# Business Outlook

GDP statistics are released in an unadjusted form.

U.S. exports destined for south of the border plunged in the first half, including a 17.6% fall in the second quarter vs. a year ago. In fact, the U.S. is bearing nearly the entire burden of Mexico's efforts to turn last year's trade deficit into a surplus, even though Mexico still has big deficits with other countries.

Canada also has slowed its buying of U.S. goods. But second-quarter exports to Canada are still up a healthy 11.5% from a year ago. In Japan, trade reform and the strong yen have allowed some market inroads. Exports to Japan are up 23% over the year.

**HOW WILL THE DOLLAR'S** new strength affect trade? The greenback was rising even before the aggressive central-bank intervention. Indeed, the August action worked because it complemented market forces. As a result, the dollar was trading in mid-August at six-month highs of 1.467 marks and 97.6 yen (chart).

The dollar has been helped by expectations of lower interest rates abroad and the renewed net inflow of foreign capital into U.S. bond and equity markets. Those conditions should continue in coming months.

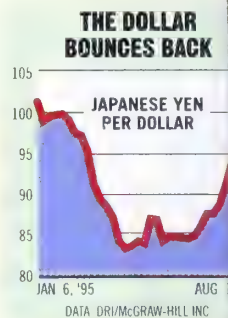
In fact, the Federal Reserve left short-term interest rates unchanged at its Aug. 22 meeting, holding the federal funds rate at 5.75% as expected. In Germany, meanwhile, a rate cut by the Bundesbank became a surer bet when the M3 money supply took an unexpected

drop in July. The important inflation gauge fell below its average of 1994's fourth quarter.

At the same time, Japan has liberalized its restrictions on international transactions, in the hopes of fixing its financial system and weakening the yen. Toll moves should help to stimulate Japan's economy, add more support to U.S. exports. Moreover, the yen's recent deterioration is already equivalent to an interest-rate cut of 1.5 to 2 percentage points by the Bank of Japan, says William Sterling, chief strategist at BEA Associates, a fund-management group.

As long as the dollar stays below 100 yen, it will have only muted effects on U.S.-Japan trade flows. Imports will become a bit more attractive, and exports will come under some price pressure.

The bigger problem is that the consequences of the rising dollar may reinforce the dangerous trend in U.S. trade. As long as imports continue to grow despite slower U.S. growth, the trade deficit remain a millstone around the expansion's neck.



America Online users can talk to Cooper and Madigan about the economy on Thursday, Aug. 31, at 9 p.m. EDT.

## MEXICO

### THE INCREDIBLE SHRINKING MEXICAN ECONOMY

**T**he startling depth of Mexico's recession is coming into view. Reflecting the peso's crash and austerity measures, second-quarter real gross domestic product plunged 10.5% from a year ago, after a 0.6% dip in the first quarter.

The tumble was far worse than the 7% or less that analysts expected—and the largest in the 15 years of quarterly GDP data. The government said the drop was exaggerated by 1994's strong second quarter and by fewer working days in this year's period. Private forecasters are revising their 1995 projections from a 4% decline to 5% or more.

The good news is that stringent monetary and fiscal policies have

stabilized the markets. The peso is holding at about 6.2 to the dollar.

Since March, stock prices are up more than 60%, and interest rates are down from 82% to about 35%, reflecting the recent drop in the

monthly inflation rate, from 8% in April to 2.04% in July. Fresh foreign capital—crucial to a recovery given the dearth of bank credit—is trickling in again.

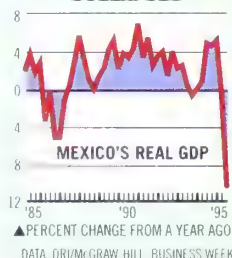
Mexico now has more than enough funds to pay off its outstanding tesobonos—dollar-indexed securities. Official capital inflows, mainly loans from the U.S. and the International Monetary Fund, will more than offset net capital outflows this year, and the 1995 trade sur-

plus may end up large enough to balance the current account.

But amid draconian interest rates, cuts in government spending, and a 50% hike in sales tax, companies have laid off nearly 1 million workers. The official jobless rate was 6.6% in June. Unofficially, unemployment is closer to one in four. Consumer spending, 70% of GDP, has plummeted, with June retail sales off 28% from a year ago.

Analysts expect a further, if less nasty, decline in third-quarter GDP. Meanwhile, President Ernesto Zedillo Ponce de León is under pressure to loosen the austerity reins. The financial markets eagerly await his first State of the Nation address on Sept. 1, but policy easing is limited by IMF loan guidelines and by the markets' stern discipline.

#### THE ECONOMY COLLAPSES







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INSTRUMENTS**



## MEDICINE

# BYPASSING THE TRAUMA

A novel technique promises to take the "open" out of heart surgery

Each year, half a million Americans endure open-heart surgery and learn firsthand that its name is far too gentle for a procedure so violent: Surgeons must make at least a foot-long incision in the chest and crack open the sternum just to get near the heart for a typical bypass operation. Even when the repair works perfectly, the painful recovery from such trauma can take months, with risks of infection and other complications.

Now, a Silicon Valley startup has pioneered what could be the most significant advance in heart surgery in decades: Over the past five months, surgeons at Stanford University have used technology from Redwood City (Calif.)-based Heartport Inc. to perform single-bypass procedures on three patients—without ever opening their chests. Rather, they made a handful of tiny incisions and used a series of novel catheters, sophisticated imaging microscopes, and other special instruments to operate through narrow tubes, or "ports."

It's a revolutionary approach, and early results are cause for great optimism. Although the first patient, on Apr. 1, developed a complication that required further surgery, the next two

walked out of Stanford Medical Center in just a few days. Stanford has more surgeries scheduled, and heart surgeons elsewhere are eager to try the technique. "This is a tremendous advance," says Dr. Greg H. Ribakove, a cardiovascular surgeon at New York University Medical Center. Surgeons "should cause the least amount of pain and trauma for the most amount of help, and that's what this is," he says.

Just as important, the "port-access" procedure, which Heartport was set to announce Aug. 24, could jolt the multi-billion-dollar economics of heart surgery. Today, hospitals charge from \$20,000 to \$60,000 for open-heart procedures. Port access promises to reduce hospital stays and limit complications, likely lowering costs for insurers and employers footing the hefty bills. Says Michael J. Strauss, president of Washington-based reimbursement consultants Health Technology Associates: "The potential to improve patient outcomes and save resources is huge."

**CAUTIOUS.** Within three months, medical centers at NYU and Johns Hopkins University will begin performing these procedures; another half-dozen major institutions are lining up to follow. For now, though, the nascent operation is being



performed only on single-bypass patients. Heartport Chief Executive Wesley Sterman notes the procedure will likely stay in clinical testing through 1995. Such testing is crucial: Uneven training of surgeons has complicated and delayed the adoption of many new technologies, and high-profile flops with port access by overanxious docs would be disastrous. Sterman vows to move cautiously, but current progress continues, he expects the Food & Drug Administration to

## NO PAIN, BIG GAIN

*New "port-access" heart surgery could provide dramatic benefits over traditional open-heart operations:*



### ◀ PORT ACCESS

4-7 tiny incisions

7-10 hours\*

Alert within hours

2 days

1-2 weeks

Unclear, but should be significantly lower

\*Eventually should decline to





**ON THE SCREEN** Stevens tracks his progress on a monitor as he operates on a heart patient with surgical instruments that he helped design

port the green light to work on complex bypass operations, as well as live surgeries and eventually, most procedures.

Heartport's heart surgery is the latest string of impressive "minimally invasive" procedures that have transformed many surgical procedures in recent years. The challenge: The risk of infection and difficulty of recuperation is directly related to the extent of trauma surgery. So medical researchers

have focused on making patients happier and cutting costs by disrupting healthy tissue as little as possible. Small-incision surgeries have become standard for removing diseased gallbladders, as well as for orthopedic operations that can put athletes back on the field within weeks.

As visualization technologies have improved, surgeons get increasingly clear, even three-dimensional looks inside the body, allowing them to precisely manip-

ulate long-handled instruments through tubes. In this way, they can complete a bypass operation just as they would through an open chest: In each of Heartport's three surgeries, an existing artery was detached from the chest wall, then spliced and stitched into a diseased coronary artery, allowing blood to bypass a blockage.

But rather than having to wire the rib cage back together and close the huge incision, surgeons just made a few quick stitches at each port, most of them a centimeter or two wide. Heartport patient Paul C. Vogel of Saratoga, Calif., says that just a couple of hours after his surgery, he felt almost no pain. The next morning, the 55-year-old retired Lockheed Martin Corp. administrator walked to the waiting room to visit with his twin granddaughters.

Heartport founders Sterman and Dr. John H. Stevens, both 35, were Stanford medical school classmates and friends in the mid-1980s, and they watched as technology made a growing list of surgeries safer. After snagging his M.D., Sterman veered off to business school, then worked briefly in venture capital; Stevens pressed on and became a heart surgeon at Stanford.

They kept dreaming of making cardiac surgery less traumatic, but a huge biological obstacle blocked the way. Most open-heart procedures require surgeons to stop a beating heart and hook up tubes and machines that take over the organ's job during surgery. The risk of working on a wiggling, throbbing mass of heart muscle is extremely high in an open procedure—and would be virtually impossible through ports.

**KEEPING COOL** The two doctors founded Heartport in 1991, based on a hunch on how to overcome the beating-heart problem. After huddling with other clinicians and an engineering team, Sterman and Stevens developed special

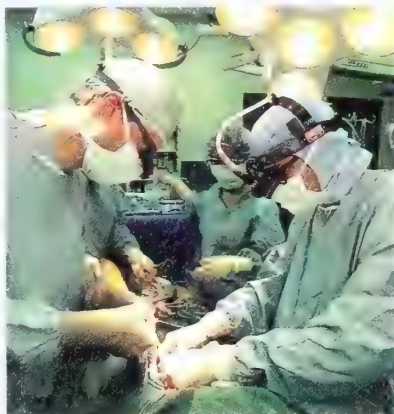
catheters that snake up through veins and arteries in the groin. In hundreds of trial runs with animals, they refined a technique of applying chemicals through these catheters that temporarily stopped the heart and kept it cool. Other tubes recirculated the blood through external machines.

After the first procedure, Stevens re-

## OPEN HEART ►

|                        |                                                                         |
|------------------------|-------------------------------------------------------------------------|
| <b>INCISION</b>        | One 12- to 15-inch incision, requiring opening the sternum and rib cage |
| <b>OPERATING TIME</b>  | 4 hours                                                                 |
| <b>COMFORT</b>         | Substantial pain                                                        |
| <b>HOSPITAL STAY</b>   | 5-7 days                                                                |
| <b>RECOVERY PERIOD</b> | 4-12 weeks                                                              |
| <b>COST</b>            | \$20,000-\$60,000                                                       |

DATA: HEARTPORT





fined the techniques, shaving almost three hours off his operating time in the subsequent two surgeries. It's no cakewalk: Even with the heart still, surgeons must get used to doing this work in tight quarters and through surgical scopes, he explains. Heartport also developed novel sutures and instruments, such as cauterizers armed with their own tiny vacuums to suck smoke out. Stevens admits his first procedure was

"scary" because of all the new variables. Medical technologies are a hot property on Wall Street these days, and Stermann says he's swamped with calls from bankers who would like to take Heartport public. The company has no competition now, and Stermann claims he has a raft of patents and pending claims on the technology. But he plans to wait until 1996 for an initial public offering, partly because the company is well

funded, having raised \$25 million. A blue-ribbon venture-capital firm, including Kleiner Perkins Caufield and Partners and Sierra Ventures, Crows is partner Petri Vainio: "This has the potential to be the medical device of the decade." Not to mention who it could mean for hundreds of thousands of very sick patients.

By Joan O'C. Hamilton in Redwood City, Calif.

## REGULATION

### WILL HEALTHIER BIRDS MEAN SICKER PEOPLE?

Giving poultry an antibiotic may make it useless to humans

**W**ith drug-resistant strains of bacteria proliferating wildly, doctors treasure the few antibiotics still capable of knocking out dangerous diseases. They try to use them sparingly to reduce the chances that bacteria will develop resistance. Doctors are especially protective of new synthetic antibiotics called fluoroquinolones—the only drugs left that can conquer certain virulent strains of dysentery and typhoid fever. One type is being deployed against an epidemic of dysentery in Zaire, Burundi, and Rwanda that's killing 15% of its victims.

That's why some public-health officials were alarmed on Aug. 18 when the Food & Drug Administration approved the use of a type of fluoroquinolone—sarfloxacin—against bacterial infections in poultry. They worry that the move will make sarfloxacin ineffective against human disease: Bacteria in poultry will become resistant to the antibiotic, and then could pass on the trait to other bacteria that cause diseases such as dysentery. "We're very concerned," says Mitchell L. Cohen, director of bacterial and mycotic diseases at the Centers for Disease Control (CDC) in Atlanta.

Skeptics also question whether the benefits of the FDA move warrant the risk. Feeding chickens and turkeys sarfloxacin, which is sold by Abbott Laboratories under the brand name Sarflox, isn't intended to make poultry safer to eat: the strain of *E. coli* bacteria it controls doesn't harm people anyway. Rather, by saving infected flocks, it

may slightly reduce the supermarket price of chicken—and, not incidentally, help the profitability of poultry producers. "The industry is very pleased," says Steve Pretanik, director of science and technology for the National Broiler Council, trade group for the \$15 billion chicken production and processing industry. Abbott Labs declined comment.

The FDA says it's aware of the threat

usually in the U.S. "We intend to regulate this very strictly," said Stephen Sundluf, director of the FDA's Center for Veterinary Medicine.

Poultry producers, plus a good number of academics, say the emergence of drug-resistant bacteria that harm people is solely due to overuse of antibiotics in treating human infections. "The use of antibiotics in animals has very little if any impact on human health in man," says Virgil W. Harrison, a retired professor from the University of Kentucky's animal science department. As evidence, he says that farm animals who spend time near humans don't seem to have a higher occurrence of antibiotic-resistant infections.

But many doctors argue that the lack of proof of a linkage is the result of inadequate research. They say a bacterial

strain that withstands sarfloxacin is likely to develop resistance to the whole class of fluoroquinolones. Says Dr. Stephen B. Levy, a professor of medicine and of molecular biology and microbiology at Tufts University School of Medicine: "Just keep using the antibiotic, and the resistance will come."

**WEIGHING RISKS.** Levy worries that once farmers begin to use how effective Sarflox is, they won't want to limit their use of it. Agricultural sales of antibiotics already total some \$1 billion a year (chart), and volume, roughly equal to the amount used by humans, if antibiotics weren't used for growth promotion in animals, retail prices for chicken and pork might be 1% to 2% higher, economists say.

But some scientists, including Gary Cassell, a University of Alabama microbiologist who studied the topic for the congressional Office of Technology Assessment, question whether such efforts outweigh the risks to human health. Given the potential perils, skeptics wonder, is it really so important to save 2¢ on a pound of chicken?

By Lars Hansen in New York



from drug-resistant bacteria. In a first, the agency will monitor use of the antibiotic with the CDC and the Agriculture Dept., and may halt its use if resistance develops. Use of the antibiotic also will be limited: It can only be used to treat outbreaks of disease in poultry, not as a preventative. And just 38 veterinarians will be allowed to prescribe the antibiotic—for an estimated 2% of the 7.5 billion chickens and turkeys produced an-



# JOHN FINALLY MAKES IT TO THE BIG LEAGUES

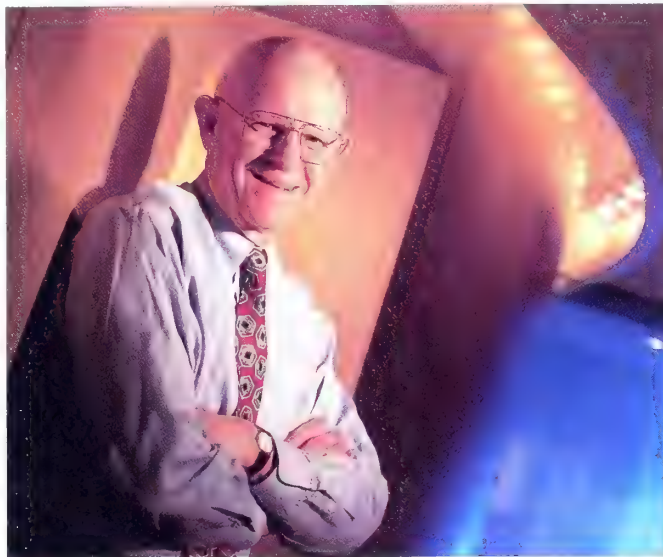
CEO Zabriskie engineered the Pharmacia merger

was a stunning bit of serendipity. John L. Zabriskie, chairman of perennial takeover candidate Upjohn Co., quietly searching for a merger partner last March. The top of his list was Zeneca's Pharmacia. But before he made a move, Zabriskie received a surprise phone call at his Kalamazoo (Mich.) home. On the line was Pharmacia's Chief Executive Jan Ekberg.

Ekberg was calling to propose a U.S. distribution deal, Zabriskie had grander ambitions. The courtship culminated Aug. 20, when the companies' boards voted for a "merger of equals" financed by a tax-free stock swap. If shareholders approve, the merger would transform two mid-tier drug companies, Pharmacia & Upjohn Inc., into a global player analysts say is destined to double its earnings by 1997.

**NEW ERA.** The deal is a triumph for Zabriskie, who would become CEO of the new company. He enticed Ekberg into a agreement that had eluded other European drug companies. He also persuaded the Upjohn family, which owns 25% of Upjohn's shares, to loosen their grip on the 108-year-old company. "We recognize we're being distanced from our heritage, and that tugs at me," said William U. Parfet, grandson of founder W.E. Upjohn and a company director. "But this is absolutely the right thing for Upjohn to do in today's environment, and John Zabriskie is really the key."

Only the second nonfamily member to lead Upjohn, Zabriskie landed there in January, 1994, having left industry leader Merck & Co. when he learned he wouldn't win its top job. The 56-year-old organic chemist arrived eager to push Upjohn into the pharmaceutical big leagues. But the situation was bleak. Upjohn Chairman Theodore Cooper had died unexpectedly, and the company was facing the expiration of patents on four



JOHN L. ZABRISKIE

## AGE 56

**EDUCATION** BS chemistry, Dartmouth College; PhD organic chemistry, University of Rochester.

**FIRST JOB** Joined Merck & Co. as a chemist, then took jobs in quality control, manufacturing, and marketing.

**FAST TRACK** Named a Merck senior vice-president in 1991, heading manufacturing. Elected executive vice-president in 1993; considered a candidate to replace P. Roy Vagelos as CEO.

**NEW TRACK** Joined Upjohn as chairman and CEO in January, 1994, succeeding Theodore Cooper.

**TRACK RECORD** Cost-cutting lifted Upjohn's 1994 profits by 25%, but revenue remains flat.

drugs worth \$400 million in revenue.

Zabriskie slashed costs, eliminated 1,400 jobs, and sold off noncore assets such as Asgrow Seed Co. Says Walter Trosin, a former Merck vice-president who worked closely with Zabriskie. "Upjohn needed an outsider to come in and tear down some of their fiefdoms." Upjohn got just that: Earnings jumped 25% last year, to \$491 million, despite flat sales of \$3.3 billion.

Zabriskie understood, though, that cost-cutting wasn't enough. In the spring and summer of 1994, he huddled with Upjohn's top 20 executives at Brooke Lodge, the summer home of the company's founder located just outside Kalamazoo. They sketched out a plan

to catapult Upjohn into the ranks of the top 10 drugmakers by 2000—in large part by finding a merger partner. The tricky part: convincing the board. In September, 1994, Zabriskie began methodically laying out his plan to directors. "John orchestrated the discussion so that...it wasn't just his views, take it or leave it," says Parfet, who relayed details to other family members. Zabriskie warned that inaction left Upjohn vulnerable to raiders. By November, the board gave him the green light.

**OF LIKE MINDS.** So when Ekberg made his call out of the blue four months later, Zabriskie was ready. Although Ekberg wasn't phoning to talk merger, he, too, was gunning for the top 10. He, too, had slashed expenses to keep the maker of cancer drugs profitable. When Ekberg arrived in 1986 at Pharmacia's predecessor company, KabiVitrum, finances were so bad he had to borrow \$12.5 million to make payroll. By last year, operating profits were \$726 million on sales of \$3.6 billion.

Zabriskie proposed a meeting at the Willard Inter-Continental Hotel in Washington, D.C., which led quickly to a string of private meetings at hotels in London, Paris, and New York. "As Jan and I talked, we realized we shared a common view of what it takes to succeed," Zabriskie recalls. Adds Ekberg: "It was an excellent fit."

The deal still could be upended by a hostile bid—a possibility that pushed both companies' shares up after news of the merger. But Pharmacia has a built-in takeover defense: the Swedish government's 14% stake and Volvo's 28% holding. The two big investors scotched previously proposed acquisitions by Rhône-Poulenc Rorer Inc. and Zeneca Group PLC. Upjohn's family holding, with employees' 10%, poses another formidable barrier.

So Zabriskie, who just finished restoring a historic home in Kalamazoo, expects to move to Pharmacia & Upjohn's new London headquarters early next year. And he relishes the thought of closing in on his old employer, Merck. "I can't wait until they're chasing me. I would love it." He'll have to find two or three more Pharmacia mergers to realize that scenario. But a man can dream.

By Keith Naughton in Detroit and Heidi Dawley in London





## LABOR

# BELL ATLANTIC: PLAYING CHICKEN ON THE I-WAY

It wants to pay workers less to install and service networks

**B**ell Atlantic Corp. Chairman Raymond W. Smith long has seen himself as a soaring visionary who intends to be a pioneer of the Information Age. Bell Atlantic has aggressively pursued such ideas as wiring homes with fiber optics and video on demand.

Now a powerful labor union may drag Smith back to earth. In recent weeks, the six other Baby Bells have signed new pacts with the Communications Workers of America (CWA) that give union members the right to work on the fiber optics likely to be the backbone of the Information Superhighway.

Smith is having none of the union's demands. Bell Atlantic wants to pay I-way workers 40% less than the \$40,000 a year CWA members get for phone work. It wants to subcontract work to cheaper suppliers. Plus, it says the other Bells' pay hikes are just too high (table). The union opposes the demands and worries that giving in would prompt requests for concessions from other Bells.

A nasty, drawn-out strike looks increasingly likely: Bell Atlantic's contract expired on Aug. 5 and the CWA can walk out any day. In preparation, the union has earmarked \$5 million for a massive campaign of negative advertisements and to get pension funds to dump the compa-

ny's stock. The union is even threatening to oppose the telecommunications deregulation bill pending in Congress. So far, though, the company shows no sign of budging. "Bell Atlantic has always led the way for the other Bell operating companies, and I think we'll do that again with our labor agreements," says Tyler Williams, Bell Atlantic vice-president for labor relations.

The heart of the dispute concerns jobs that may be created to build and service the I-way. Not much of this work is under way yet, although Bell Atlantic and other Bells have some experiments going. But long-term, many believe homes will be wired into fiber-optic networks, which will carry phone calls as well as services such as video on demand. Fearing their current jobs may barely exist, CWA members want to ensure they do

## GOING IT ALONE

### BELL ATLANTIC

- ▶ 4% pay hike over three years plus \$2,600 in bonuses
- ▶ 40% lower pay scales for all Information Superhighway work

### OTHER BABY BELLS

- ▶ 10.5% to 11% pay hike over three years plus up to \$3,300 in bonuses
- ▶ 25% to 40% lower pay scales but only for some Info Highway jobs

**UNDER THE GUN:** The CWA is threatening to oppose telecom reform

I-way work at their current wage. Bell Atlantic argues that the \$20-an-hour wage for technicians makes it uncompetitive with lower-paying union cable companies. To level the playing field, management wants all I-way work performed at a customer's home done by newly created unionized subsidiaries that would pay \$8 to \$12 an hour. It wants to subcontract more work to lower-paying outside suppliers. So far, Bell Atlantic has farmed out nearly 4,000 jobs, leaving 37,000 union members.

**WIGGLE ROOM.** The CWA says it's willing to horse-trade to make Bell Atlantic more competitive. Officials don't believe that most cable workers are direct rivals. U S West Inc. actually raised wages for some technicians after finding that its higher-skilled workers earned less than similar cable company workers. Still, the CWA says it will give Bell Atlantic the 40% lower pay scales, but only if the jobs are returned to current union wage levels should phone and I-way lines ever merge. As an alternative, the CWA wants an end to all subcontracting.

The union thinks it has left the company wiggle room. "I've probably gone further than most members would like me license to do, but I'm willing to let what it takes to avoid a war," says Peter G. Catucci, the vice-president in charge of the CWA's bargaining. But Koeppe, president of Bell Atlantic in New Jersey, who is overseeing the company's bargaining, says these ideas "have a great deal of promise."

Other Bells, however, are happy to pay far less than Bell Atlantic is demanding. The other Bells did win lower pay scales on less-skilled I-way jobs, even though they got nothing close to Bell Atlantic's demands. "The sum of the agreement makes us very competitive," says Pacific Telesis Group labor relations director Robin G. Macgillivray.

Bell Atlantic is well-positioned to stand a long walkout. It is one of the most profitable Bells, and much of its network is automated. However, the CWA's \$90 million strike fund would allow it to hang in for a long time, too. If Bell Atlantic wins, its rivals could be scrambling to catch up. But the result is a costly labor war that nets little, Smith's I-way dream could be disrupted by some sleepless nights.

By Aaron Bernstein in New York, with Peter Burrows in San Francisco



# HOW CONVERSE GOT ITS LACES ALL TANGLED

lost \$41.6 million in 85 days on clothing maker Apex One

Corporate acquisitions don't always work out as planned. But to buy a company and then shut it down at a loss after just 85 days deserves a sort of booby prize.

This year's award goes to chagrined executives at shoemaker Converse Inc. On May 18, they trumpeted the acquisition of Apex One Inc., a leading maker of sports apparel. On Aug. 11, Converse abruptly shuttered its new unit, citing expectedly slow orders and high

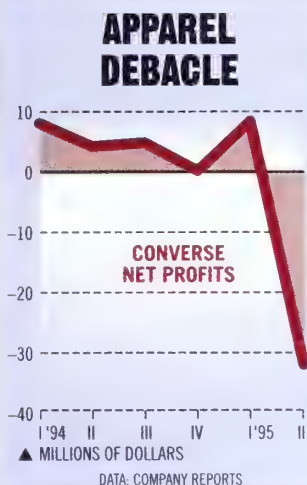
costs. The fiasco has been costly: Converse took a \$41.6 million pretax loss on its Apex investment in the second quarter, weakening its already shaky balance sheet. Apollo Advisors, the New York investment firm run by Leon D. Black, is egg on its face, as Apollo controls Converse, and its executives closely involved in overseeing the purchase.

The finger-pointing is already begun. A spokesman for Apollo says Converse "management was making decisions, with input from the CEO." For his part, Converse CEO Gil "Gib" Ford says Apex' sales were below the projections made by its managers last spring. He's hinting at a possible legal action. Meanwhile, Apex' Operating Officer David Koontz says Converse and Apollo simply didn't understand Apex' situation and tried to find a wrong fix. Apollo's executives, he says, were clearly in charge of the unit yet "don't know the apparel business from a bar of soap."

Before its bizarre final chapter, Apex was a Cinderella of the sports apparel industry. Founded in 1988, it spent big to secure sponsorship deals with the National Football League and popular sports franchises such as the Dallas Cowboys and New York Giants. The pacts gave Apex the right to design unique apparel for the teams and players to wear on the side-

lines. The idea: Fans would see the gear on TV and rush out to buy "authentic" \$120 warm-up jackets and other goods.

Amid a boom in licensed sports clothing, Apex surged to \$50 million in sales in 1992 and \$100 million in 1993. By 1994, it had partial or full deals with nine NFL teams and had expanded into other sports. Trouble was, Apex was a lot better at marketing and designing than it was at delivering goods. The privately held company was undercap-



## Before its bizarre final chapter, seven-year-old Apex was a Cinderella of the sportswear industry

talized and constantly had to scramble for money to pay suppliers. The problem peaked in late 1994, when many retailers barely received anything, while others got shipments weeks late. Although Apex executives say they had orders worth \$150 million in 1994, they delivered just \$102 million worth. A 1994 net loss of \$48 million sealed Apex' fate.

**CRASH EFFORT.** By the time Converse bought the company in May for about \$35 million, Apex was nearly insolvent. Worse, retailers were so angry that it had just \$35 million in orders on the books, a third of the prior spring's backlog. Instead of sensing disaster, though, Converse executives saw Apex as a cheap way to jump into the apparel business and pick up valuable sponsorships. With Converse's backing, they believed, retailers would regain confi-

dence. According to Converse CEO Ford, Apex' managers projected that sales could rebound to nearly 1994 levels if Converse took charge.

Converse launched a crash effort to get new designs ready for delivery by Thanksgiving, with the Converse logo replacing that of Apex. "The office in Hong Kong went into a frenzy, and we actually started producing the new designs," says Koontz. Never mind that retailers had already placed the bulk of their fall and Christmas orders. Adds Koontz: "They hoped that by developing new lines, they would create excitement in the marketplace. They were looking for a Thanksgiving resurrection."

But Apex' corpse wouldn't rise to the occasion. The market was soft, and most retailers no longer trusted Apex, even with Converse's backing. "I didn't want to put too many orders with Apex and

Converse this year until they got things sorted out," says Norm Charney, president of Athletic Supply of Dallas Inc. By August, the backlog hadn't budged, and creditors were raging. Facing the need to spend up to \$25 million to keep Apex afloat, by one insider's estimate, Converse and Apollo pulled the plug.

Converse's own troubles undoubtedly played a part in the decision. Revenues dropped 14% in the second quarter, and it posted an operating loss of \$8.4 million, not counting Apex. Given that backdrop, says CEO Ford, "We felt we had to take this action to protect Converse." But the Apex write-off leaves Converse with a scary 5-to-1 debt-to-equity ratio. Some analysts are whispering that Apollo may now try to sell the company. Hardly a fruitful 85 days.

By Mark Maremont in Boston



## POLITICS

### IN '96, THREE MAY NOT BE A CROWD

With voters this disaffected, a third party may play a big role

As Labor Day approaches, it looks at first like American politics as usual: President Clinton is golfing in the Grand Tetons, taking time out for briefings on Bosnia, and generally trying to look—well, Presidential. GOP front-runner Bob Dole has rented a cottage in New Hampshire and plans a week of folksy politicking. On Sept. 1, the Kansan will launch his fall campaign with a “boatercade” on Lake Winnepesaukee, leading an armada of supporters from Weir’s Beach to Wolfeboro while camera crews bob alongside. It seems like a traditional start of a traditional Presidential campaign.

But look again. Increasingly, there are signs of public discontent with Establishment pols such as Clinton and Dole, and unease with their parties. The President’s support remains frozen at about the 43% plurality that elected him. No GOP challenger has caught fire with the electorate. And although voters triggered a revolution last November by booting Democrats out of power in Congress, new surveys find Americans disenchanted with the Republican regime.

**“FULL MOON.”** The result, says senior Dole adviser Richard N. Bond, is the kind of gnawing uncertainty a mainstream campaign abhors. “People are still shopping for alternatives,” Bond says. “There’s the [Colin] Powell thing, the Ross Perot thing, talk that [retiring New Jersey Senator] Bill Bradley may run. It’s the Presidential equivalent of a full moon.”

A new poll by the Times Mirror Center for the People & the

Press found that 26% of those surveyed now back the notion of an independent candidate, compared with 32% who favor Clinton’s reelection and 35% who prefer a Republican. Says the Center’s director, Andrew Kohut: “People are...critical of the Republican Hill leadership [45% disapprove of GOP policies, 38% approve] but don’t see Democrats as an alternative.”

### Rebirth of the Third Force

*In this century, America’s two-party system has gone virtually unchallenged—until the last 25 years.*



**1968** Alabama Governor George Wallace attacks the two parties for running “a Tweedledee and Tweedledum system.” He lands on the Presidential ballot in all 50 states.

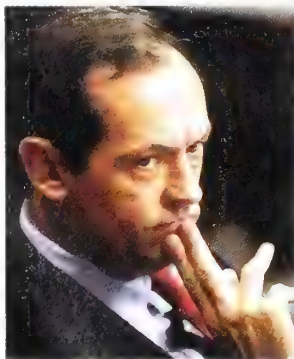
**1980** Independent John Anderson briefly harnesses voter disgust to run neck and neck with incumbent Jimmy Carter and challenger

Ronald Reagan. But his campaign fizzles, taking only 7% of the vote.



**1992** Texas billionaire Ross Perot communicates directly with voters through televised talk shows and electronic “town halls.” He stuns both parties by winning 19% of the vote.

**1993** Colin Powell retires as chairman of the Joint Chiefs of Staff. Polls show him to be one of the nation’s most popular leaders.



**Aug. 11, 1995** Perot’s United We Stand America stages a mock nominating convention, drawing every GOP Presidential wannabe and White House emissaries.

**Aug. 16, 1995** Democrat Bill Bradley announces he won’t seek another Senate term, hinting at an independent run for the Presidency.



That development is particularly alarming for the Republicans. “Sure, we are all these bills whizzing to passage,” says Sal Russo, a GOP consultant in Sacramento. “But the public doesn’t see progress on term limits and the Balanced Budget Amendment, two things they care about.” Adds GOP strategist William Kristol: “A huge amount depends on whether the first year of the new Congress is a success. If we have a chance at building a stable governing coalition. Failure would produce dealignment, independent candidates, and instability.”

Actually, given Perot’s ’92 Presidential charge, that instability may already be at hand. The root cause: post-cold-war trauma over stagnant wages, corporate layoffs, and fraying morals. “The search

for a national redeemer is characteristic of a society under stress,” says Ross Baker, a Rutgers University political scientist. “In the expression, Third Force movements popped up left and right. Today, we have a severe crisis fueled by the economic numbers.” Among the

portents:

**■ The Big Crack** While the Republicans are recasting themselves as a harder-edged, more conservative party, Democrats seem to be imploding. The Democrats now control a

minority of statehouses. And the party’s congressional wing is in turmoil as centrists revolt against their liberal leaders. Weevils such as Louisiana Representative W.J. (Bibi)

Tauzin and Senator Richard C. Shelby of Alabama have jumped the GOP. Other centrists such as New Jersey’s Bradley, Oklahoma Senator David L. Boren, Minnesota Representative Timothy J. Wirth have quit politics rather than defend a party they see as dominated by class-warfare rhetoric and the concerns of urban liberals.

“Politics is broken,” Bradley said simply, in announcing his retirement on Aug. 16—while signaling his interest in an independent Presidential bid. Indeed, former Democratic

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*-Nevada Wier,  
Photographer, Writer,  
Ethnographer*



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1 . 8 0 0 . 4 4 7 . 4 7 4 7



A man in a dark suit and tie is walking on a globe. He is holding a thin wire that extends from his hand to a tall, ornate building in the background. The building has a distinctive Thai architectural style with a golden spire. The globe is tilted, showing a mix of yellow, orange, and blue colors. The sky is blue with white clouds.

*Mark Hills, President  
PC ServiceSource*

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## COMMENTARY

By Amy Borrus

# WHAT THE U.N. WOMEN'S CONFERENCE CAN DO FOR WOMEN

surgent Gary Hart and Colorado's former Governor Richard Lamm want to invite Bradley and other Third-Path thinkers to a Denver powwow in December to chart a political course that could skirt the major parties.

■ **Powellmania.** On Sept. 18, Retired General Colin L. Powell will kick off a national promotional blitz for his memoirs—a trip that looms as the Mother of All Book Tours. A fiscal conservative and presumed social moderate, Powell is the darling of many voters seeking to bypass the party system. (In an Aug. 19 ABC News poll, he won 31% support to Clinton's 36% and Dole's 27%.)

By the time Powell stops barnstorming, on Oct. 20, he will have dominated news coverage for a month and fueled renewed talk of an independent run. Says an aide: "He'll take a serious look [at politics] when the tour ends." In the meantime, Powell is consulting with top political operatives and has let a grassroots "Draft Powell" movement take shape. Washington entrepreneur W. Ronald Evans says he has started a petition drive to put 200,000 signatures on Powell's desk by November.

■ **Perot-noia.** Although Ross Perot has turned hesitant about another Presidential bid, his movement may be more powerful without its controversial figurehead in the spotlight. Perot has given his United We Stand America affiliates the green light to put third-party offshoots such as New Jersey's Conservative Party, Oregon's American Party, and Wisconsin's New Party on the ballot. Says Rochester (N.Y.) pollster and sometime Perot adviser Gordon S. Black: "With 12 to 14 states having alternative political parties with ballot status and another 15 states where ballot requirements are low, you could get these groups together to field some form of Third-Force ticket next year."

Will all this ferment produce a viable alternative to Republicans and Democrats? Maybe not in time for the 1996 elections. But that's not to say the stress cracks in the established parties won't produce a rupture down the road. "The dominant parties have grown old and fat, but their institutional power remains great," cautions Paul Green, a political scientist at Governors State University in University Park, Ill. "Powell is the Third Force's best shot. But in reality, it would take Jesse Jackson's charisma, Ross Perot's money, and Bill Bradley's brains to transcend the obstacles to an independent run." Volunteers, anyone?

By Lee Walczak, with Douglas Harbrecht and Mary Beth Regan, in Washington

**F**or women's rights activists throughout the U.S., Beijing's selection as host city for the U.N.'s Fourth World Conference on Women has been a sore disappointment. China is a notorious abuser of human rights, and its record on promoting the status of women is mixed at best. Moreover, China's detention of American rights activist Harry Wu on spying charges has led to calls on Capitol Hill for a U.S. boycott of the meeting.

But holding the conclave in Beijing may turn out to be a blessing in disguise. The media hoopla generated by the gathering of 50,000 people already is shining a harsh light on China's treatment of girls and women. True, under communism, China has nearly wiped out prostitution, and female literacy rates have doubled, to 70%. But China still has a policy of forced abortion. And its one-child-per-family dictum has often meant abandonment and neglect for girl babies in a culture that favors boys.

**PROGRESS ALREADY.** The U.N. conference, which begins Sept. 4, is already having a positive effect. Embarrassed Chinese leaders on Aug. 7 unveiled a five-year plan to improve women's lives. Its aims include putting more women in top government posts, protecting women from sale into forced marriages, and halting the gruesome practice of leaving girl babies to die of neglect in dank orphanages.

Meanwhile, all the criticism of China threatens to obscure the broader aims of the U.N. conclave. Discrimination against women is a serious global problem. Women represent

two-thirds of the world's illiterate and 70% of its poor, according to a new U.N. report. Domestic violence is the leading cause of death globally for women aged 14 to 44.

The U.S. has a major role to play in making sure the U.N. conference leads to concrete gains for women worldwide. First Lady Hillary Rodham Clinton should stay home unless

the Chinese release Wu from prison as Washington has demanded. To flip-flop now would be viewed in Beijing as weakness and on Capitol Hill as kowtowing. However, the U.S. still will field a high-powered delegation that includes Madeleine K. Albright, the U.S. representative to the U.N., and Secretary of Health & Human Services Donna E. Shalala.

Despite the U.N. reputation in America for ineffectiveness, it often makes a difference in the developing world where it has greater prestige. Pressure from women's groups at

the U.N.'s 1985 women's conference in Nairobi helped pave the way for national crackdowns on violence against women in many countries. Brazil, for instance, now has special police stations for battered women seeking shelter. And Egypt gave recognition to women's groups for the first time after a U.N. conference on population control in Cairo last year. China's abysmal human rights record and Sino-U.S. tensions make it awkward to hold a women's conclave there. But this confab may yet help improve the lives of women in many parts of the world.

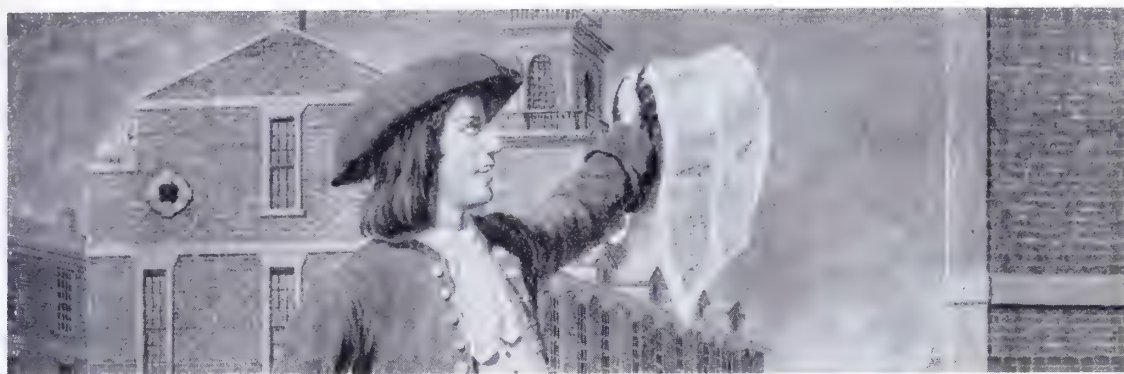
Amy Borrus covers international issues from Washington.



## WRONG SEX

A Chinese girl abandoned by her parents to die. Beijing belatedly is taking steps to halt the practice

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## DEALS

# ARE THOSE MARIE OSMOND DOLLS REALLY WORTH \$12 MILLION?

Knickerbocker's startling runup has shorts salivating

**T**he L. L. Knickerbocker Co. specializes in kitsch. Little wonder that few noticed the \$7.8 million manufacturer of such home-shopping hits as Marie Osmond's porcelain doll collection and Annette Funicello's line of teddy bears. Then, faster than you can say "in-home painless hair removal," another Knickerbocker offering, the stock jumped from \$4 to \$46 in six weeks.

Observers can't pinpoint what caused the rapid rise. "It's shocking to me," says John D. Lane, a partner with Nutmeg Securities, an underwriter of Knickerbocker's January initial public offering. The Securities & Exchange Commission and the National Association of Securities Dealers are curious, too. Each called Chief Executive Louis L. Knickerbocker, 52, to ask about the stock. Says Knickerbocker: "All I can think of is that Rafi Khan introduced me to several institutional investors."

This isn't the first time the controversial stockbroker has jumped onto a spectacular stock rise. Khan is a La Canada (Calif.)-based Pakistani who is best known for his failed 1994 attempt to take over ICN Pharmaceuticals Inc., whose stock he once pushed before turning on management. He also is known for legal skirmishes with short-sellers and others, as well as directing institutional investors, such as St. Louis-based Kennedy Capital Management, to undervalued stocks. Another client is Norman L. Yu & Co., a Newport Beach (Calif.) money manager, who owns Knickerbocker shares. Trading has been furious. From July 25 to Aug. 16, average daily trading was 250,000 shares, nearly a third of all stock available.

Khan says his interest was sparked by Knickerbocker's foray in late June



**KNICKERBOCKER'S ANGELS:** Controversial broker Rafi Khan and Director Farrah Fawcett



into direct marketing. Ads in *Doll Reader* magazine are expected to boost sales above the \$12 million in projected 1995 revenues. Khan says he contacted clients and urged them to look at the company.

**HIGH HOPES.** But the dramatic runup may not be so easily explained. Traders and brokers say the rise is due largely to the stock's soaring short position. In June, shorts—who bet a stock will decline by selling borrowed shares in anticipation that they will repay the lenders with cheaper paper in the future—controlled 1,050 shares of Knickerbocker. By July 14, short positions were 31,440. As the stock rose, shorts had to pay up for stock to cover their bets. With only 800,000 shares available, the price climbed.

Khan insists the Knickerbocker isn't overblown—though his own rhetoric about the company sometimes seems so. "Under the right circumstances, could be a \$1,000 stock," he gushes. Others are less sanguine. "If you buy stock, you're buying hopes and dreams," says Gaines, Berland Inc. analyst Ric West. Sales are vulnerable to the fact that 98% come from one outlet: QVC, TV's home-shopping giant. When QVC's on-air exposure this spring and up

the price of Knickerbocker's ECT Ionized water purifier, sales of the product fell 73% in 1995's second quarter.

Knickerbocker is a onetime real estate developer who is now his wife, Tammy Fawcett, launched private companies that sold jewelry and creams promoted by Phyllis Diller on

Home Shopping Network in the mid-late-1980s. The companies were merged to form Knickerbocker in a January 1995, public offering, and Fawcett is on its board. One misstep: Knickerbocker no longer markets Creme de La Vie, a creation of Michael Elam, Diller's former plastic surgeon. In 1990, Elam's medical license was revoked for insurance fraud and malpractice, says the prospectus.

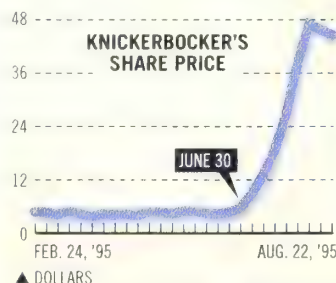
"I've seen this movie before," says John Merriman, a trader with Dabbs Resnick Inc. "Eventually, this stock will trade at \$4 or \$5 again, if you have the stomach to hang on." Still, Merriman says he is not shorting the stock. She has tangled with Khan in the past: a suit with Future Communications, a Texas cable company, they claimed manipulated both the stock supply and price. Khan's then-employer settled three suits; Khan himself took the case to arbitration. This time, if the stock tanks, the biggest loser will be Knickerbocker himself.

Some \$60 million in potential profits from his 62% stake could disappear.

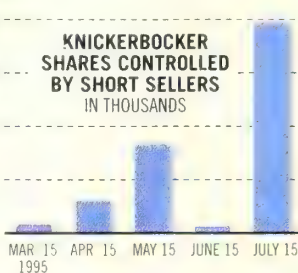
He seems unconcerned. "My goal is to take the company to \$1 billion in sales," Knickerbocker says. But that's a lofty goal for a small player in a \$5 billion industry. Almost as lofty is the stock.

By Nanette Byrnes  
Los Angeles

## A SOARING STOCK...



## ...A CROWD OF DOUBTERS



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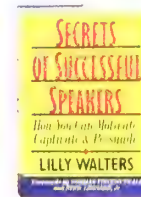
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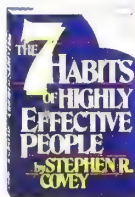
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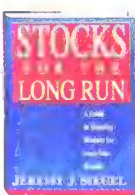
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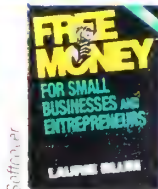
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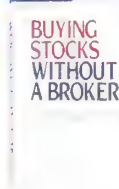
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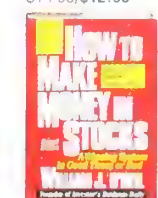
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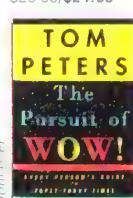
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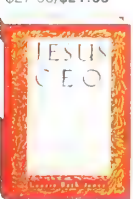
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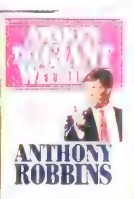
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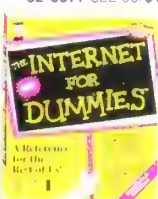
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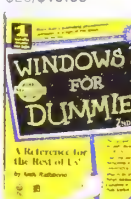
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EDITED BY KEITH H. HAMMONDS

## TURNER CAN'T GET RIP ON CBS

TURNER FINALLY BUY television network he so ts? Time Warner sources the company is abandon- efforts to unload its 18% e in Turner Broadcasting em and would back a sen- TBS bid for CBS or an- r network. That leaves one hurdle in Turner's reality. Westinghouse has up financing to back its billion agreement to buy CBS Chairman Laurence i wants cash, which Turn- does not have. General tric is talking again to er, but it won't give up rol of NBC. Don't write er off: He has, after all, d off other tough deals, as the 1985 purchase of

## CLOSING BELL

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neone—perhaps a vexed estor—couldn't wait for tember debt-rescheduling is at Eurotunnel, the Eng- Channel tunnel's cash- eezed operator. A bogus otunnel press official ned two wire services on . 22 to announce a deal n banks. The stock jumped % on the reports—after ing 17% the day before on lse rights-issue rumor. ny Eurotunnel holders, anwhile, remain underwa- Shares have dropped to 25, from \$15 in 1989.



MGM's movie library. Then again, swallowing MGM nearly bankrupted TBS.

## FORD JOINS THE CROWD IN CHINA

WHEN AUTO MAKERS LOOK AT China, they see a market where vehicle registrations are expected to triple, to 25 million, in the next decade. It's an alluring prospect, and General Motors and Chrysler already have deals to produce vehicles there. On Aug. 22, Ford established its own beachhead, paying \$40 million for 20% of Jiangling Motors. Ford will design and distribute 60,000 light trucks and vans built in central China's Jiangxi Province. The deal, which could expand to 120,000 vehicles, will get the Ford nameplate on Chinese roads by 1997.

## A \$100 MILLION GOODBYE FOR OVITZ

THE ABDICATION OF MICHAEL Ovitz is all but complete. His Creative Artists Agency on Aug. 23 announced the formation of a nine-person managing director committee, led by three co-chairmen, to run the agency after Ovitz departs Oct. 1 to become president of Walt Disney. Agents and top executives at CAA, which represents the likes of Tom Hanks, Kevin Costner, and Steven Spielberg, still are working out a plan to buy the agency from Ovitz and his two founding partners, Ron Meyer and Bill Haber. The likely price tag: more than \$100 million.

## WALL STREET IS EDGY ABOUT INTEL

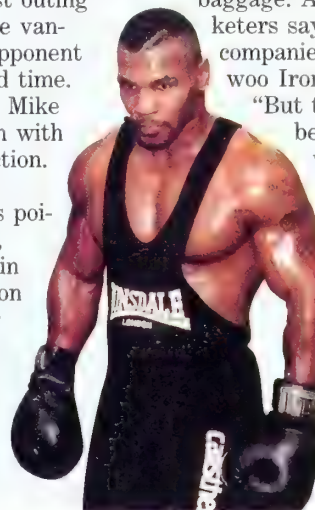
SO WIN95 IS HERE, AND SALES of Pentium chips are booming. Then why is Wall Street antsy about Intel? Its shares tumbled 7% on Aug. 21, after

## HEADLINER: MIKE TYSON

## EX-CONS DON'T PITCH PEPSI

It's a saga Madison Avenue would love. The former champion returns to his sport after a long layoff. A record number of fans plunk down \$40 apiece to watch his first outing on TV. And he vanquishes his opponent in near-record time.

But this is Mike Tyson, a felon with a rape conviction. To corporate sponsors, he's poison. Trim, fit, and a terror in the ring, Tyson bashed Peter McNeeley on Aug. 19. But don't expect a repeat of the days when he



drew \$2 million a year to pitch wares from the likes of Pepsi-Cola.

Tyson could be worth \$8 million a year in endorsements were it not for his baggage. And some marketers say there may be companies that want to woo Iron Mike's fans.

"But they'd have to be willing to write off the mainstream," says Lesa Ukman, editor of *IEG Sponsorship Report*. So far, nobody's ready to take that punch.

By David Greising

four analysts made tiny adjustments to earnings forecasts. Rational? Not really. But with chip stocks up more than 100% this year, "there are lots of people out there trying to sound prudent," says First Boston's Jack Geraghty. Some investors worry about Intel's growing sales of PC boards, which carry gross margins of roughly 15%, compared with 70% for Pentium. Never fear: The boards are packed with Intel chips and their sales lift total profits.

## SHUTTING OUT THE WIN95 NOISE

FORGET, IF YOU CAN, MICRO-soft and Windows 95 mania just for a moment. IBM and Apple Computer have spent billions on their own personal-computer operating systems. How do they cope with Win95, the most-hyped computer product introduction of all time? They lie low. "It's

something that you just don't try to counter," says Lee Reiswig, general manager of IBM's Personal Software Products division. Reiswig's group ran a three-page ad on the eve of Microsoft's Aug. 24 launch, listing hundreds of customers already using its rival OS/2 program—then took the next day off. Apple's subtle ads delivered Microsoft mock congratulations (spelled C:ongrtlns.w95). It also sent out T-shirts with the slogan: "Been there, done that."

## ET CETERA...

- The Fed left short-term rates alone, and markets took the non-move in stride.
- Roadway Services will spin off its sluggish, \$2 billion less-than-truckload business.
- ICI Explosives agreed to plead guilty to price-fixing and pay a \$10 million fine.
- Justice subpoenaed tire-makers as part of an industry antitrust investigation.



Our position, word by word.

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ED BY LEE WALCZAK

## HOW IT'S BILL S. BIG BAD BUSINESS

Democrat has courted business with the ardor that Bill Clinton displayed during the first half of his term. He alienated much of his liberal base to back deficit reduction trade-expansion pacts, key goals of Corporate America. Thanks to Clinton's trusted counselor, Thomas F. "Mack" McLarty III, the White House became a place where CEOs a problem could get a sympathetic hearing. And Commerce Secretary Ronald H. Brown turned his department into a floating bazaar to hawk U.S. exports.

Well, McLarty is still schmoozing, and Brown is still hustling. The President's fondness for his business chums has cooled in the wake of the Republican takeover of Congress. With a tough reelection race ahead, Clinton is reprising the outsider act of his '92 campaign by blasting excess lobbyists and their GOP allies. In charge: In the murky light of congressional backrooms, influence is being peddled to the highest bidder.

**THREAT.** Clinton's war on Gucci is partly personal, partly political. They say the President is miffed that, despite his wooing, CEOs overwhelmingly sided with House Speaker Newt Gingrich's anti-lobbyist radicals. Clinton also hopes to capitalize on polls indicating that—despite the GOP victory on Capitol Hill—Independent swing voters still believe Washington is dominated by organized interests. Lobbyist-bashing has other virtues as well. The White House has six GOP-backed pieces of legislation under veto. Some prime targets: banking and telecom reform. Depicting these high-profile measures as the handiwork of greedy lobbyists makes their rejection more justifiable to voters—and could force business to cough up concessions. Clinton's New Populism was on display on Aug. 8, when he flew to Baltimore. Framed by the grimy backdrop of the former Steel Corp. smokestacks, he railed against the

"brazen display of...special-interest groups" that, he claimed, misled House Republicans to gut environmental safeguards.

According to White House Chief of Staff Leon E. Panetta, the broadside is part of a campaign to depict the GOP-controlled Congress as a place where corporate interests prevail over working-class concerns. "Lobbyist friends are telling me that you have to be stupid not to take advantage of what's happening on Capitol Hill," Panetta says. "For a price, you can just about buy any legislation." Replies Tom Korologos, a business lobbyist with GOP ties: "Somehow, it's O.K. for unions, Common Cause, and Friends of the Earth to be in the backroom writing bills" for Democrats, but it's taboo for business lawyers to play the same role.

Clinton isn't alone on the attack. Vice President Al Gore has assailed House-passed telecommunications legislation as riddled with sweetheart provisions that were "sold to the highest bidder." Gore alleges that lobbyists for cable-TV companies and the Baby Bells turned the bill into an anticonsumer measure that will hike rates and reduce competition.

On Aug. 4, Clinton upped the ante. He announced he was issuing an Executive Order that would bar executive-branch employees from meeting with special-interest representatives who don't publicly disclose their clients. White House polls believe such tactics will resonate with Ross Perot supporters, who could hold the balance of power in November '96. At the very least, the Presidential blitz will put the capital's pinstriped legions on the defensive. One key GOP strategist concedes the party's lovefest with business could indeed backfire. "It hasn't yet," he says, "but I hear it ticking." So can Bill Clinton, who has decided that some of the same folks he served coffee and canapés to last year make irresistible targets now.

*By Susan B. Garland, with Mary Beth Regan*



**NEW MOOD:** War on Gucci Gulch

## CAPITAL WRAPUP

### TAX GOING FLAT?

While the GOP's official line on a radical revamp of the tax code is full steam ahead, some Republican lawmakers are getting cold feet. Senator Alfonse M. D'Amato (R-N.Y.) worries a flat tax would slash home values up to 25% by eliminating deductions for mortgage interest and local taxes. And the conservative Heritage Foundation wants to focus its fire on loopholes in the current tax code. GOP members fear that other fissures will divide the ranks.

### CLIMBING OUT OF WINDOWS

►The Justice Dept.'s probe of Microsoft Corp.'s Windows 95 has lost one of its top litigators. Antitrust attorney Jeffrey Blumenfeld left when Justice decided not to file suit against Microsoft in advance of the Aug. 24 launch of Win95. While Justice says the private attorney had a conflict of interest with other clients, sources speculate Blumenfeld may have had a falling out with chief trustbuster Anne K. Bingaman, whose probe is continuing.

### SPRUCING UP THE OLD EOB

►The General Services Administration is lobbying for an \$80 million renovation of the Old Executive Office Building, home to the President's staff. The GSA says the century-old building—adjacent to the White House—is falling apart: Water pipes leak, and the electrical system is so creaky that building engineers fear it could cause a fire. But White House officials fret that a costly upgrade now might become a partisan target for budget-slashing Republicans.





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## TAIWAN

# BEIJING'S DANGEROUS GAMES

Its military exercises give Taiwan the jitters—and pose a tough test for the U.S.

**F**ew Taiwanese politicians have a stronger pedigree in the ruling Kuomintang, or Nationalist Party, than Chen Li-an, 58. Chen's father served as vice-president under Generalissimo Chiang Kai-shek after the KMT's 1949 retreat from mainland China. Following in his father's footsteps, the younger Chen quickly rose through the ranks of key government posts.

But on Aug. 17, just two days after China launched a new round of military exercises in waters north of Taiwan, Chen shocked his compatriots by announcing he would defect from the KMT and oppose its candidate, President Lee Teng-hui, in elections next March. Sitting in his Taipei office in front of a statue of the Buddhist goddess of mercy, Chen says he made his bold move in part because Lee's triumphant visit to the U.S. in June has backfired, drawing Chinese wrath. "The military demonstrations make all of us think how we can avoid making mistakes we all will regret," he says.

**CROSSFIRE.** Chen's defection is just one of the shock waves China is sending through Taiwan, which Beijing regards as a renegade province (table). Since the People's Liberation Army announced in July that it would begin firing missiles near Taiwan, the local stock market has plunged 12%. The New Taiwan dollar has hit a four-year low of 27.45 against the greenback. Economic growth forecasts have been scaled back half a percentage point, to 6.5%. "No measures to upgrade the Taiwan economy can proceed under the present circumstances," says John Nelson, head of investment research for Jardine Fleming Taiwan Securities Ltd.

China's exercises, involving naval and air units and live artillery drills just 95 miles from Taiwan, are a problem for

## HOSTILE MOVE

The Chinese maneuvers include firing missiles into the waters north of Taiwan



## HOW CHINA'S SABER-RATTLING IS SHAKING UP TAIWAN

- Creating a crisis within the ruling Kuomintang over policy toward China
- Forcing the government to reconsider its high-profile campaign to win broader international recognition
- Contributing to a 12% decline in Taiwan's stock market
- Creating new tensions regarding Taiwan's investments on the mainland, forcing Taiwan companies to shift investments to Vietnam, the Philippines, and Indonesia
- Preventing the establishment of direct air and shipping links between Taiwan and China



than just the island's 21 million people. Japan and Southeast Asia already have been jarred by China's underground position of a nuclear device this summer and by its expanding claims in the South China Sea. Former U.S. Ambassador to China James R. Lilley says Beijing's action will cause "an escalation in arms race all over Asia."

The Chinese saber-rattling also spells trouble for U.S. policymakers. Though Boeing, Ford, Lockheed Martin, AT&T, and other U.S. companies are proceeding with new sales or deals, the Clinton Administration is caught in a bipartisan fire over managing relations with China. That has left it zigzagging

sure to dissuade voters from supporting Lee and to put the brakes on a budding independence movement. "They'll continue with exercises until at least March, and maybe have a big one right before the election," says one Western military attaché. This could anger Taiwan's powerful supporters in Congress, inflaming Washington's perennial China debate. "We have a moral obligation not to abandon Taiwan," says Washington hard-liner Frank J. Gaffney Jr., director of the Center for Security Policy. "We have a strategic interest in not acquiescing to Beijing's expansionist impulses."

By manipulating Taiwan's politics, China hopes to expand a key fissure in-

wan. Taiwanese companies have invested more than \$20 billion in China, and they increasingly fear Beijing will take those investments hostage. Applications for major investment projects on the mainland have dropped 40% in a month.

Taiwan executives are looking for ways to persuade Beijing to soften its military tactics. On Aug. 14, two of Taiwan's Cabinet ministers met with several of Taiwan's most powerful business leaders to find ways of jump-starting a dialogue with Beijing. "We still have leverage with our investments," says Parris Chang, a legislator with the Democratic Progressive Party, the leading opposition party and a major advocate of independence.

But the leverage may not work. Because of the nationalist mood in Beijing, the Chinese seem willing to accept economic hardships resulting from a pull-back by Taiwanese investors. "China is saying they're willing to bite that bullet, to lose investment along the coast," a Western diplomat in Beijing says. "They're saying that Taiwan is an overriding issue of sovereignty."

**GOOD BUY.** A surprising number of foreign investors in Taiwan argue that the crisis will simply pass. To them, the panic among local, mostly individual investors has made the Taiwan stock market an attractive buy. On Aug. 21, Solomon Brothers Inc.'s weekly research report advised investors to triple their Taiwan equity holdings, from 2% to 6% of their Asian portfolios. "Most people are looking at this as a short-term phenomenon," says Timothy Greeton, fund manager for Credit Lyonnais International Asset Management Hong Kong Ltd. In mid-August, he beefed up the Taiwan percentage of his Greater China Fund from 15% to 20%.

But most of Taiwan's residents aren't so confident. By trying to influence the elections in Taiwan, Beijing is playing a dangerous game. "Once Communist China starts, I don't think they'll stop," says Jaw Shau-kong, a mainland politician who also has defected from the KMT to become secretary-general of the rival New Party.

Clearly, the problem isn't going away. Taiwan's growing assertiveness and China's increased willingness to use military means to intimidate the island appear to be long-term trends fundamentally at odds with each other. The dangers of accidents or miscalculations can only grow. If the voices of independence in Taiwan make big gains, the U.S. and East Asia could get caught up in a new and potentially dangerous stage of confrontation across the Taiwan Straits.

*By Bruce Einhorn and John Winzenburg in Taipei, with Dexter Roberts in Beijing and Stan Crock in Washington*



between conciliation and confrontation (p. 42). For now, the Administration has a sanguine view of events in the South Straits. Officials in Washington here is no prospect that China will fully blockade or invade Taiwan.

**WING SPLIT.** But in Beijing, Western analysts say the Chinese are preparing months of steadily intensifying military pressure against Taiwan. That's why because Communist Party boss Jiang Zemin and other leaders are rallying around the cause of reunifying with an as part of their maneuvering to speed paramount leader Deng Xiao-

An immediate goal is to influence the outcome of Taiwan's presidential elections in March. The Chinese suspect that Lee and other Taiwan-born politicians are leading the island away from even reunification and will formally assert independence. As Taiwan basks in international recognition, the cause of greater international recognition is increasingly popular among voters and cuts across both generational and political party lines.

Beijing-based diplomats expect the pressure to keep ratcheting up the pres-

**TWO CHINAS?**  
President Lee and his backers may have less interest in reunification than do old-line KMT politicians



side the KMT between politicians with family roots on the mainland and their Taiwan-born colleagues. The mainland contingent worries that Lee's attempts to rejoin the U.N. and gain international recognition mean that he secretly supports *taidu*, or complete independence for Taiwan. Lee, who just weeks ago seemed a shoo-in to win the March election, now faces deepening opposition as a result of the growing split. While he still leads in opinion polls, his numbers fell from 45% to 37% after Chen's bombshell announcement.

There are also huge business stakes in the face-off between China and Tai-



## INDIA

# ENRON: MAYBE MEGADEALS MEAN MEGARISK

The India project isn't the only one that seems to be stalled

It has been a rough few weeks for Rebecca P. Mark. On Aug. 3, the chairman and chief executive of Enron Corp.'s international-power unit had her biggest deal, in India, abruptly canceled after a state government review. Mark's effort to salvage the \$2.8 billion Dabhol project with last-minute promises of concessions only produced scorn from Hindu nationalist politicians. Then, back in the U.S., on a vacation to unwind, she was tossed into a cactus while on a horseback excursion.

Mark, 41, says she has shaken off her setbacks and is confident of resuscitating Enron's contract to build the 2,015-megawatt Dabhol power plant. But the Indian rejection is raising questions about the \$9 billion Houston energy giant's global strategy and its hard-charging style. By quickly developing big overseas projects and then selling off stakes, Enron hopes to maintain strong profit growth. But some of its grandest efforts, such as a natural-gas pipeline from Bolivia to Brazil and power plants in Turkey and Indonesia, remain deadlocked over such issues as the price of power, the degree of private ownership, and whether such projects are even viable.

Enron is determined to show that its global push continues unabated. Mark goes to Bolivia soon for talks on the pipeline, and she has already returned to India, where Enron has invested some \$200 million, to testify before its Parliament. "We're not sitting here wringing our hands," she explains.

**GEOMETRICALLY MESSIER.** That message is important to Wall Street, which has pushed Enron's stock down by 10%, to 33%, in the last two months. Until then, many analysts had considered the stock to be undervalued. Since 1988, Enron's sales have doubled, and earnings have expanded 15% annually for the past four years. Enron had scored big successes in Britain and South America, and a slew of major projects such as Dabhol is in the works. Altogether, Enron is involved in discussions on some \$10 billion

in power plants and pipelines in South America, Asia, and the Middle East (table). This year, Mark's international unit is expected to contribute \$180 million in pretax profits, 16.5% of Enron's total, vs. 4% in 1992.

But as most Western developers are finding, completing megaprojects in emerging markets is enormously more difficult than building small ones. "There is tremendous fear by governments on big projects that they might make a mistake and have to live with it for 15 years," says James J. Steele, chief executive at Houston-based Mosbacher Power Group and a former Enron development executive. China, which with India is expected to account for up to 40% of global growth in power capacity, has delayed dozens of large, privately financed plants over squabbles about in-

vestor guarantees and rates of return. Malaysia has even banned new plants to prevent overcapacity.

Enron's Indian Dabhol debacle, however, has been the biggest shock. When Enron first got involved in 1992, the new reformist government, led by Prime Minister Narasimha Rao, was desperate for foreign investment in infrastructure. A month after meeting touring Indian officials in Houston, Enron sent executives to India. They delivered a memorandum of understanding in just 10 days to build a massive power complex.

**"SHAMBLES."** Eighteen months later, Maharashtra State Electricity Board agreed to buy 90% of the power Dabhol produces. The financial terms and ownership structure "were not ideal," India, concedes an official in India's power ministry. "When we accepted the project, we were in shambles," he adds. "We had no investors."

But Enron made some miscalculations. The most fundamental was political. It didn't take seriously a rising backlash against foreign investment, an opposition coalition led by the Bharatiya Janata Party. During its campaign for state elections in February, 1993, the BJP called for a reevaluation of the Enron project. Instead of waiting



**UNDAUNTED:** "We're not sitting here wringing our hands," says Mark



vote's outcome, Enron rushed to close the deal and began contention—apparently thinking that it would make it difficult for a new government to unwind the deal. Enron just blasted on," says a State Dept. source familiar with the deal. "Public perception didn't concern them."

It should have. The BJP coalition in Maharashtra and quickly led its promise. "They had agreed to review the project, and doing so would have been difficult," says Srinivasan Subramanian, an India representative of stock exchange HG Asia. The problem compounded when the U.S. Energy Dept. in June issued a statement warning that killing the deal could adversely affect U.S. power projects. A diplomatic source says Enron "pushed like hell to get Energy to issue the statement. But Indian politicians immediately attacked the statement as an attempt by Washington to threaten India. "These kinds of statements are actually threats, and it didn't help Enron at all," contends BJP economic adviser Jay Dubashi.

Another apparent faux pas was not coming up with a local partner. Enron's only co-investors were General Electric Co. and Bechtel Group, both U.S. companies. What's more, Enron



**THANKS, BUT NO THANKS:** Local protests pushed Bombay politicians to cancel a big Enron deal

had quietly arranged to sell a 20% stake in Dabhol to New Orleans-based utility Entergy Corp., which likely would have drawn more fire. Enron officials maintain that the Indian government advised it not to enlist a domestic partner for fear of showing favoritism to certain Indian companies. But the absence of allies created the appearance that the foreigners were milking India.

The deal's secrecy didn't help, either. Dabhol was one of eight plants placed on a "fast track" by New Delhi. Besides getting government loan guarantees, the projects were awarded without competitive bidding. Enron's rate of return was estimated at 23%, far higher than the 16% over capital costs guaranteed to others by the Indian government. Critics also thought the 7.4¢ per kilowatt-hour that Enron would get for the power was high. Enron fought to keep the details confidential, but a successful lawsuit by a Bombay consumer group forced disclosure. When Enron offered to renegotiate to make the power

cheaper, critics cited that as proof it had padded costs in the first place.

Enron is having more success building small power plants, such as a 110-Mw facility in Guatemala and two others that already operate in the Philippines, where Enron was a pioneer when most foreign investors shied away out of fear of political risks. And in China, Enron has broken ground on a 150-Mw plant on Hainan Island. "We've been as successful in this business as anyone," says Mark.

**DRAGGING ON.** But Enron's major focus is on megaprojects, which is what it needs most to meet financial targets and keep investors happy. With gas prices depressed in the U.S., earnings are getting a big boost from sales of its holdings in international-power and pipeline projects. For instance, dividends in Britain's Teesside plant and other projects helped push up net income 24%, to \$94 million, in the six months ended

June 30. But for this strategy to work, Enron must complete projects and sell off stakes—and do so quickly. With negotiations still dragging on from Indonesia to Turkey to Brazil, it will be a challenge for Enron to maintain its schedule. While the company says it won't take a write-off on Dabhol, it has already held up, if not halted, the sale of a 20% stake to Entergy.

If Enron can't get Dabhol back on track, other important plans could be affected. The company is counting on India to be a primary market for a huge processing plant for liquid natural gas (LNG) that it's building in Qatar. Mobil Oil Corp., which already has a similar plant in Qatar, has rights to the biggest LNG markets, such as Japan and South Korea. Enron says it has enough alternative markets to India, but some analysts are skeptical. Enron also maintains that losing Dabhol won't hurt its growth forecasts. The plunge in its stock, though, shows investors are worried.

Mark isn't giving up on India. She still believes Enron can come to terms with the Maharashtra government. Lately, the BJP has been putting more blame on the ruling Congress Party (I) than the U.S. company for the deal. Many observers in India think the BJP will renegotiate, then use the deal to their political advantage by showing that they managed to broker a fairer contract. But even if Enron can salvage Dabhol, it can ill afford many more complications of the same magnitude.

*By Gary McWilliams in Houston and Sharon Moshavi in New Delhi, with Michael Shari in Jakarta and bureau reports*

## Enron's Global Scorecard

| PROJECT                                           | COST<br>BILLIONS | STATUS                                                               |
|---------------------------------------------------|------------------|----------------------------------------------------------------------|
| 1,120-mile liquid-natural-gas (LNG) pipeline      | \$3.0            | Delayed by feud between World Bank and Brazil over foreign ownership |
| Build and operate 150-Mw plant on Hainan Island   | \$0.1            | Under construction                                                   |
| Two-phase 2,015-Mw LNG-fired plant in Maharashtra | \$2.8            | Canceled                                                             |
| Build and operate two LNG-fired plants            | \$0.7            | Negotiations stalled                                                 |
| Two small power plants in Subic Bay and Batangas  | \$0.1            | In operation                                                         |
| Plant to process 5 million tons of LNG            | \$4.0            | Negotiations under way but viability questioned                      |
| 480-Mw plant in Marmara                           | \$0.5            | Negotiations ongoing                                                 |

DATA: SALOMON BROTHERS INC., COMPANY REPORTS



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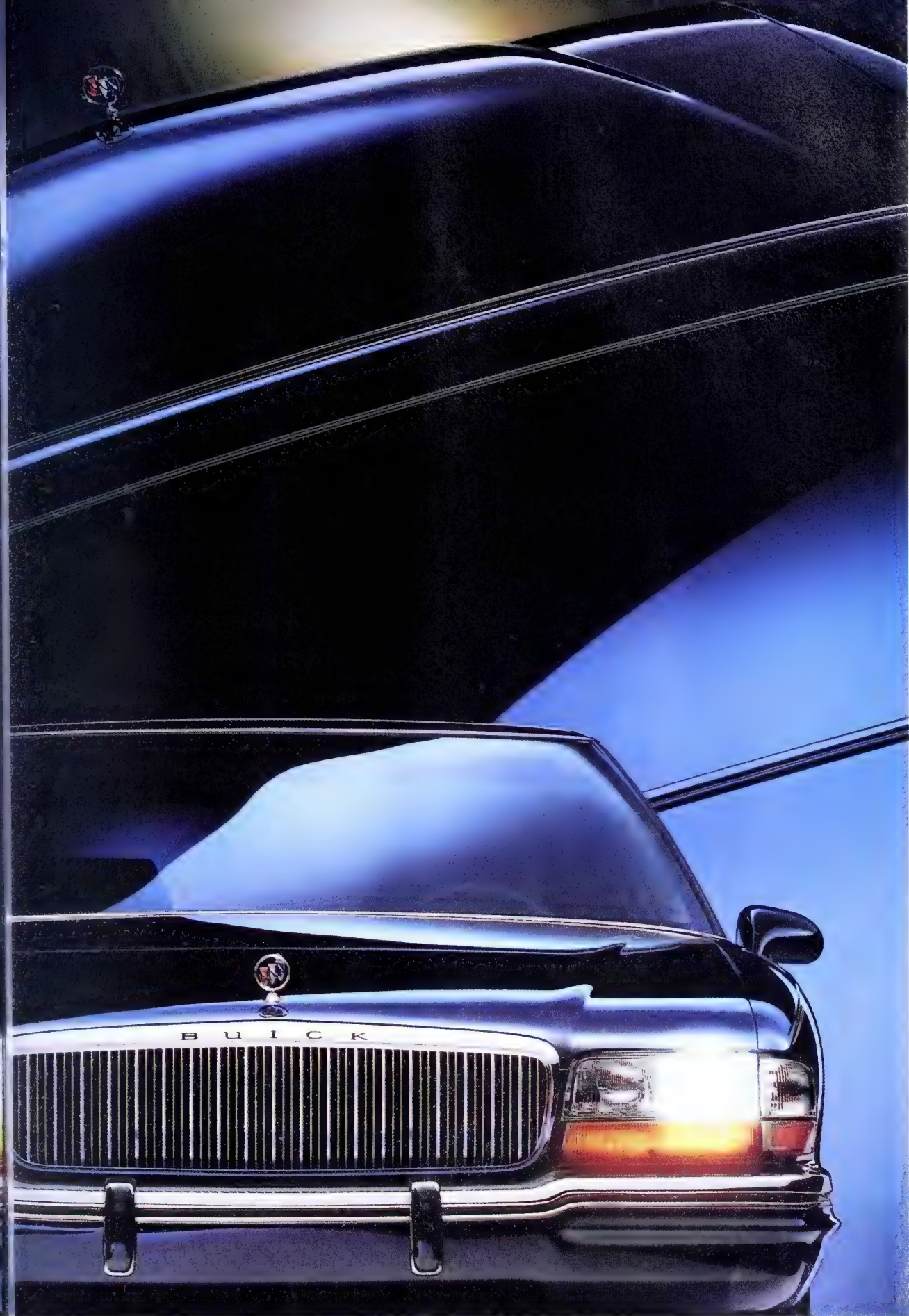
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## CHERNOMYRDIN'S STAR FADING EVEN FASTER THAN IT ROSE?

Only a few months ago, Viktor S. Chernomyrdin was riding high. The Russian Prime Minister's success in negotiating release of Russian hostages from Chechen rebels made him look like a leading contender for the presidency—especially since President Boris Yeltsin's health and popularity have been fading fast. Western policymakers were ready to see a solid, if unglamorous, successor in the wings. In a month is a long time in Russian politics. As the gears up for parliamentary elections on Dec. 17—followed by presidential elections in June—Chernomyrdin is already running into trouble. His new political party, Our Home Is Russia, was tested in its first electoral test in a regional ballot on Aug. 12. One reason for voters was persistent economic trouble, still severe enough to spur the government to appeal to the International Monetary Fund for an \$18 billion loan. Meanwhile, a new political star is rising: Former General Alexander Lebed, an outspoken populist and nationalist, has come out on top in new public opinion polls. **NOT TO LOSE.** For Chernomyrdin, the upshot could be the opposite of what he hoped for when he set up his party in May. Instead of consolidating his power base, Our Home may end up with no more than 15% of the seats in the new member Duma, analysts predict. That could give Chernomyrdin's opponents—or even Yeltsin—a chance to call for resignation on the grounds that he failed to win a mandate. Says Moscow political consultant Sergei Mikhailov: "Chernomyrdin has a lot to lose."

The Prime Minister's dilemma is partly a result of Russia's nascent democracy. As many as 100 political parties are expected to take part in the December elections, confusing

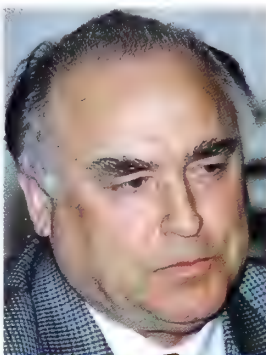
voters. The centrist Our Home party was set up with Yeltsin's endorsement to create the basis for a two-party system in Russia. Made up of federal bureaucrats and high-level local officials, it was dubbed "the party of power."

**RATINGS SLUMP.** Now, that's a liability. "Chernomyrdin's bloc is seen as the status quo, so everyone will run against it," says Michael McFaul, an analyst at the Carnegie Endowment for International Peace in Moscow. Even Yeltsin has distanced himself from Our Home, keeping his options open. Although Yeltsin's approval rating has slumped to a dismal 4.8%, Kremlin observers say he wants to run again next year. Some believe Yeltsin might even call off the presidential elections if he decides he can't win.

Over the next few months, Chernomyrdin will be cranking his party's campaign into full gear. With support from businesspeople, Our Home seems on track to raise from \$20 million to \$50 million in campaign funds. The trick will be transforming that money into votes. In the 1993 elections, business gave more than \$200 million to the Russia's Choice party led by Yegor T. Gaidar, but nationalist Vladimir V. Zhirinovskiy gained the most votes. Zhirinovskiy may win fewer seats this time as voters switch to Lebed.

To come out of the December ballot stronger, Chernomyrdin has to emerge as one of the top two vote-getters. For now, the betting is that the election may lead to a virtual stalemate: five or six parties sharing almost equal blocs of seats in the Duma. That would throw the presidential race wide open. So both Westerners and Russians should be prepared: It may take many more political fights to decide who—if anyone—succeeds Yeltsin.

*By Patricia Kranz in Moscow*



**CHERNOMYRDIN:** The target of discontent

**LEBED:** The ex-general leads in recent polls



## GLOBAL WRAPUP

### GERMANY'S CRACKDOWN

Germany's first insider-trading conviction under a year-old law bolsters confidence by Frankfurt officials that Germany can create more transparent financial markets. Federal authorities indicted Harald Kronseder, a member of the founding family of beverage-maker Krones, \$1.3 million. Kronseder sold \$800,000 worth of shares last November before Krones revised its profit forecasts downward. More penalties may be on the way. Authorities are extending their

probe to employees of Commerzbank, which is Krones' bank. Altogether, the 65-person securities watchdog team has launched 16 investigations. "This is all part of building a new equity culture in Germany," says Georg Wittich, head of the Federal Supervisory Office for Securities Trading.

### TOKYO UPROAR

► A Moody's Investors Service study on Japan's fragile banking system has sparked a furor in Tokyo. Moody's new rating system—from A for excellent to E for desperate—suggests

that Japan's debt-laden banks are in more trouble than originally thought.

Moody's assigned 10 of Japan's 50 major banks its lowest rating. Japanese bank execs were quick to criticize the ranking, which drove the Nikkei down by 1.4% on Aug. 21.

But Moody's isn't the only worried watchdog. Standard & Poor's, a unit of The McGraw-Hill Companies, publisher of BUSINESS WEEK, has placed five banks on its Creditwatch list for a possible downgrade. The International Monetary Fund has also found Japan to be slow in tackling the crisis.



## SPORTS

# A THREE-WAY JUMP BALL IN THE NBA

If dissident players scrap the union, the season could be lost

**F**or more than a decade, the National Basketball Assn. has enjoyed peace and prosperity while baseball and football bounced from one labor catastrophe to the next. Now, the NBA, too, is teetering at the edge of a nasty labor battle.

The central problem is one most employers and employees would love to have: how to split up a fast-growing pie. Dissident players, led by superstars Michael Jordan and Patrick Ewing, think the new six-year pact the basketball players' union and the NBA reached in mid-August would undercut players' ability to sell their services to the highest-bidding team.

**SHOWDOWN.** Instead, they want players to decertify the union. The idea isn't necessarily to dump it permanently but to clear the way for suing the NBA on antitrust grounds, which players can do if no union exists. This would force owners into a better deal, they say, just as an antitrust suit against the National Football League scored football players a better contract a few years ago. Meanwhile, the NBA fired a preemptive shot by locking out the players.

Showdown time is coming in early September, when the National Basketball Players Assn.'s 425 members will vote on decertification. If a majority says no, players will likely approve the new pact, which lowers their share of total revenues to 48%. But if players say yes to a decert, the league will face a dilemma. It could sweeten the pot. Or it could continue the lockout, as Commissioner David J. Stern vows to do, and run the risk of a worse contract—plus potentially huge antitrust damages—down the road. Both sides would lose big if basketball ends up replaying a disaster like baseball's last year.

So far, the players' vote is too close to call. Some 200 players signed decert petitions this summer, but others think the strategy is too risky. "Decertification gets you nowhere but into a courtroom," says Utah Jazz guard John Stockton. Says Los Angeles agent Leonard Ar-

mato: "Labor strife causes irreparable harm to the sport, like in baseball." He's advising clients such as Orlando center Shaquille O'Neal to vote no.

Until now, the key to basketball's labor peace has been the salary-cap system agreed to in 1983. That pact limited total player pay to 53% of NBA revenues, vs. the 60% they had been getting. However, teams could use half a dozen exceptions to pay over the cap. The



**SHAQ O'NEAL: STICKING WITH THE UNION?**

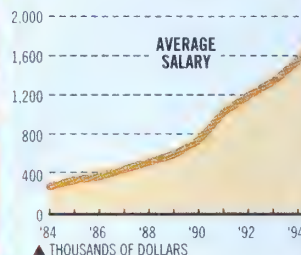
loopholes kept salaries climbing at double-digit rates, even as revenue growth slumped from 20% a year to less than 10% in recent seasons.

The result: Average salaries have quintupled in the past decade, to \$1.87 million last season. The NBA argues that this amounts to 64% of revenues, way over the cap. Meanwhile, leaguewide pretax margins collapsed from a peak of \$195 million in 1993 to about \$70 million last season, says the NBA. "We can't afford to go on like this anymore," says Commissioner Stern.

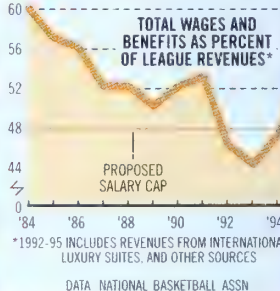
So Stern proposed what he argues is a 59% salary cap, a limit on roster pay, and fewer exceptions. And he urged the union to back a so-called luxury tax on teams that spend beyond the cap. But when dissidents threatened to decertify, the league rescinded the proposal. In mid-July, the union agreed to a new proposal. But Jordan and company still balked and have continued the decert campaign.

Why are the dissidents still griping? They argue that the proposed system takes away so many salary-cap exceptions that it would undercut the market for players, who can sell their skills to the highest-bidding team in three years. Fewer teams could bid a dollar for players they want. And players' ability to switch teams for a better deal would be curtailed. Teams would have less room to maneuver since they're already way over the

## AS PLAYER SALARIES SOAR...



## ...OWNERS WANT TO CAP THEM



cap. "A fair deal begins with what we had before," says Chicago Bulls guard Michael Jordan. "We won't go back from that."

The dissidents also don't buy the NBA's stats. The old agreement's definition of revenue left out income from luxury boxes, international TV, and advertising billboards, which was either minuscule or nonexistent in 1983. But this revenue boomed in the early 1990s. The union even won a legal settlement against owners for excluding this income.

Once these items are included, as owners agreed to do in the proposed





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the numbers look completely different. Players got about 53% of the expanded revenues last season, the NBA concedes, vs. 64% of the narrower revenue definition. And the new salary cap works out to 48% of the expanded revenue. In other words, the previous system cut the players' share to way below the old 53% cap (chart, page 58). When salaries shot up to the cap last season, owners de-

cided that 53% was too high after all. The question players face is how hard to press for more. Union President Simon Gourdine embarked on a national tour in mid-August to drum up support for the new contract. But Gourdine's fear of playing the decent card left him looking weak after the dissidents' threats prompted owners to kill the luxury tax he had agreed to. Militant players argue

that the NBA is just as worried as the union about winding up in a baseball-style mess. So the league will cave some more if they decertify, they argue. The risk is that the owners may cede their ground. Fans may soon need lessons from their baseball brethren about how to survive without a season.

By Aaron Bernstein in New York  
with Kevin Kelly in Chicago

## COMMENTARY

By Christopher Farrell

# WHY SOME COMPENSATION IS CLEAN OUTTA SIGHT

**T**he numbers are staggering. Actor Sylvester Stallone gets \$20 million a movie, and baseball's Barry Bonds some \$7 million a year. Walt Disney Co. Chief Executive Michael D. Eisner's total compensation was \$10.6 million last year—and \$203 million in 1993.

These astronomical sums contribute to one of the most wrenching trends in American society: widening income inequality. For instance, the average CEO now earns about 53 times as much as a factory worker, up from some 42 times in 1980. Today, more than 200 baseball players rake in at least \$1 million a season. In 1980, only one did—Nolan Ryan. Stars are taking home outside rewards not only when measured against workers. In every industry and profession, stars earn more money than ever compared with peers in their field.

**MULTIPLIER.** Why is talent today reaping so much more than a decade ago? The answer may lie in the impact of communication technologies operating in the global economy, which has vastly multiplied the rewards to talent and reputation. University of Chicago economist Sherwin Rosen calls it the "economics of superstars." Economists Robert H. Frank of Cornell University and Philip J. Cook of Duke University label this phenomenon "winner-take-all markets" in their book, *The Winner-Take-All Society*.

Here's the idea. It has always been the case that everyone would like to listen to the best singers and watch the best cinematic heroes.

Similarly, in the high-stakes business world, every board of directors wants the fiercest, smartest, and best-regarded chief executive it can find. Indicted for murder? Hire the best lawyer. And so on.

What's different now is that markets keep getting bigger and bigger. In almost every industry, from entertainment to software to consulting,

yer—fame that can only enhance his potential to earn big bucks. Their professions may differ, but the economics underlying their stratospheric paychecks is the same.

**CAREER LOTTERY.** The surge in celebrity income can be both bad and good. The lure of dollar signs can lead thousands of youngsters to squander the energy on what amounts to winning

an occupational lottery, such as becoming a professional athlete or a movie actor. On the other hand, superstar income can propel economic growth. Look at the business heroes of the 1990s, such as Microsoft Corp.'s billionaire founder, William L. Gates III. Thanks to him and hundreds of other high-tech stars, hordes of enterprising people are starting their own companies and developing new technologies. Many of them will fail, but their entrepreneurial efforts

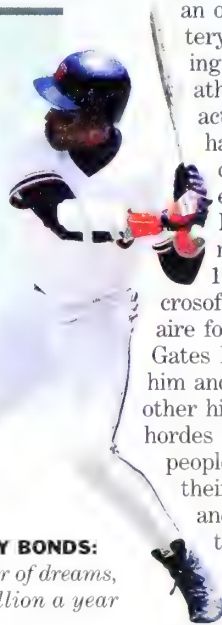
## Winner Takes All



**SYLVESTER STALLONE:**  
*After Judge Dredd,*  
\$20 million a movie



**MICHAEL D. EISNER:**  
*Disney CEO, \$10.6*  
million last year



**BARRY BONDS:**  
*Fielder of dreams,*  
\$7 million a year

international business is growing in significance. Even mostly local businesses such as electric utilities compete on a larger national and international stage. Whoever gains star status—through skill or luck—has the leverage to get a big chunk of the action.

Many of today's superstars are going global. Eisner runs a worldwide media behemoth. Arnold Schwarzenegger's action films are hits in the U.S. and overseas. Barbra Streisand reaches millions through the global technologies of radio, records, television, and satellite hookups. Cable TV has transformed Johnnie L. Cochran Jr. from a local Los Angeles figure into the world's most prominent law-

are building the new information economy.

Today, global commerce is roaring ahead, as the developing world and the former East bloc embrace free markets. Communications technologies are forging stronger links between nations and peoples. You had better get ready for even bigger star salaries tomorrow.

Farrell is a *BUSINESS WEEK* economics editor.

Power Macintosh  
Artists Don't  
Just Draw Pictures



Imagine having the power to do all the things that a Macintosh  
encoding from workstation-plus speeds. The power to push not  
To see video run on your computer, but the limits of your creativity  
on your television. To publish in minutes what once took hours. To have  
that contain photos flexible enough to change when your needs  
and graphics. The freedom to grow. The freedom to adapt. It's  
businesspeople comes with the Power Macintosh 9500. The heart  
series, you have the most powerful desktop publishing solution ever created.







# One only thing more powerful than a Macintosh is your imagination.

## The new family of Power Macintosh computers.

Introducing the new family of Power Macintosh computers. The professional Macintosh family. Faster than a thought. More powerful than a burst of inspiration. And more powerful than any computer in the world.

Never been given so much room to grow. These machines lie the rocks-like-a-hurricane PowerPC architecture. That the new, ultrahigh-performance 604 RISC chip is as fast as a dual 100 MHz Pentium chip. It's also built onto a single-board architecture, ensuring you an easy upgrade path. And, when you're concerned, the true test of a computer's power is what it can do with it. And in the case of these machines, it may very well be what you can imagine.

The Power Macintosh 9500 is the heart of the most powerful publishing system on a desktop. Your favorite software runs faster than ever before. You produce results faster than ever before. And we've added standard PCI architecture for even greater flexibility. With the horsepower, the Power Macintosh 8500 flies through jobs like CAD/CAM, 3-D modeling and 3-D rendering. It has video-in/video-out capabilities, as well as CD-quality audio. It's never been easier to create on-line movies in minutes.

Imagine having the performance. Low-end price. It's what makes the Power Macintosh into something you can't live without. Like all Power Macintosh computers, it's as easy as you are with built-in high-speed Ethernet networking. For creative solutions, SC means more power for everything you do: searching, editing, performing. Now together a videoconference, updating a spreadsheet, the functionality of a Mac OS. Everything. So you can maximize your most valuable asset on a new Power Mac. So you spend more of your time working. The shortest distance is time waiting for your computer to catch up with you.

It's not about how powerful the computer is. It's about what the computer makes you. The power to turn inspiration into reality. The power to be your best.







### **The Power Macintosh 9500.**

*120 or 132 MHz PowerPC 601 RISC processor*

*Processor upgradeable via daughterboard*

*6 PCI slots*

*3 expansion bays*

*12 DIMM sockets*

*16MB to 64MB of DRAM*

*16GB or 2GB Fast SCSI hard disk*

*Built in 10Base-T and AUI Ethernet*

### **The Apple Color LaserWriter 12/600 PS.**

*Prints 600 dpi*

*Apple Color Photocentric*

*ColorSync 2.0*

*12 ppm black 3 ppm color*

*Windows 3.1 compatible*

*Adobe PostScript Level 2*

*Built in Ethernet for Novell*

*AppleTalk or TCP/IP networks*



### **The Power Macintosh 8500.**

*120 MHz PowerPC 601 RISC processor*

*Processor upgradeable via daughterboard*

*3 PCI slots*

*3 expansion bays*

*3 DIMM sockets*

*16MB to 32MB of DRAM*

*16GB or 2GB Fast SCSI hard disk*

*Built in cache to increase output capabilities  
up to 40 frames per second*

*Built in 10Base-T and AUI Ethernet*



### **The Power Macintosh 7200 and 7500.**

*3 PCI slots*

*Built in 10Base-T and AUI Ethernet*

#### **7500**

*100 MHz PowerPC 601 RISC processor*

*Processor upgradeable via daughterboard*

*3 expansion bays*

*3 DIMM sockets*

*16MB to 32MB of DRAM*

*Built in cache to*

#### **7200**

*75 or 90 MHz PowerPC 601 RISC processor*

*3 DIMM sockets*

*For more information, call 1-800-541-0000 or visit our website at <http://www.apple.com>*

The power to be your best.

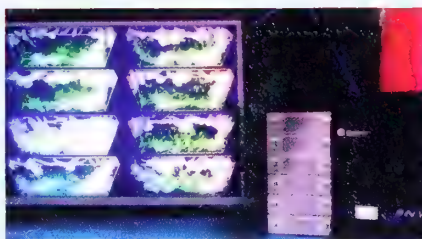


ED BY OTIS PORT

## ASSSEL OF PIXELS FOR SHARPER IMAGES

TECHNOLOGY FOR COMPUTER displays lags far behind the development of other components. The University of Minnesota's new Laboratory for Computational Science & Engineering aims to change that, armed with a \$100,000 grant from the National Science Foundation. At a supercomputing conference last November, it unveiled an imaging technology featuring 8 million pixels or dots, or pixels. That's

double the pixel count in today's best monitors. For this year's meeting, Paul Woodward, the lab's director, hopes to show off a system with 16 million pixels. That would match 35mm film quality, which is what Hollywood needs to simplify the creation of digital effects. The technology can also display multiple slices of a 3-D simulation, so scientists can study what's happening at various



depths—for example, in the tornado-like vortices near the surface of the sun.

To produce full-motion images with such sparkling resolution, the Minnesota lab harnesses multiple workstations so each handles a

different section of the image. That requires clever programming to keep the machines synchronized because it takes a few milliseconds—an eternity to

high-speed processors—for data to zip between computers. Woodward believes it may be possible to keep computers in sync even for the 30 milliseconds that data need to shuffle between machines on opposite coasts.

## AP GUITARS—GOOD VIBRATIONS

SPACE ENGINEERS MAY have discovered a way to use high technology to make inexpensive guitars. Other string instruments may sound much better. It started when Steven Griffin, who is studying for his doctorate in aerospace engineering at the Georgia Institute of Technology, started strumming a guitar. He started wondering why custom-made guitars sound so much richer than their garden-variety counterparts.

placed sensors, Griffin found that a guitar's main sound stems from the primary vibrations of the upper plate, the part to



which the bridge is attached. He found that the secondary vibrations generate the overtones that are especially pleasing to the ear. But many secondary vibrations get absorbed by the thick wood used in inexpensive guitars.

Griffin figured that technology could compensate for this damping. So he installed a small piezoelectric crystal on the upper plate, which converts a minute current from two 9-volt batteries into vibrations that help the upper plate generate the desired overtones. Next, Griffin plans to test the concept on other string instruments.

## INNOVATIONS

■ Polymer chemists usually have to be satisfied with making materials that are reactive only in a few places. In the Aug. 25 *Science*, however, Cornell University researchers led by Jean M.J. Frechet describe how they build polymers with dozens of reaction points. These polymers are shaped like trees, not chains. The extra reactive sites should produce plastics, coatings, and lubricants with a wider variety of properties.

■ A tomato a day keeps heart attacks away? Could be. Scientists at Technion-Israel Institute of Technology in Haifa believe tomatoes may contain antioxidants similar to those in red wine. These compounds reduce cholesterol oxidation, which can lead to heart attacks and strokes, by up to 70%.

■ Cooling molded aluminum parts has always been a hit-or-miss proposition. It can take weeks of experiments to find a procedure that doesn't hurt the part's performance. But now, computer simulations can determine the best quenching methods before the first part is fabricated. The new software was developed by Issam Mudawar, a mechanical engineering professor at Purdue University.

## NON GIVES POWER TO THE PUPIL

CANON INC.'S UPCOMING video recorder and 35mm film cameras, the eyes have it—control, that is. The eye-control system in the viewfinder is much more advanced than the original technology in Canon's EOS A2E 35mm camera, introduced three years ago. That system handled only focusing. The new eye-control capabilities also include "look-at" menus. With the new ES5000 video recorder, you can select

options, such as fading and strobe effects, just by staring for two seconds at a menu listing. Eye movements can handle nearly everything except zoom control. Sensors in the viewfinder determine precisely where you're looking by measuring the position of the eye's iris.

This gadgetry isn't cheap. When the ES5000 makes its debut in September, it should cost close to \$2,000

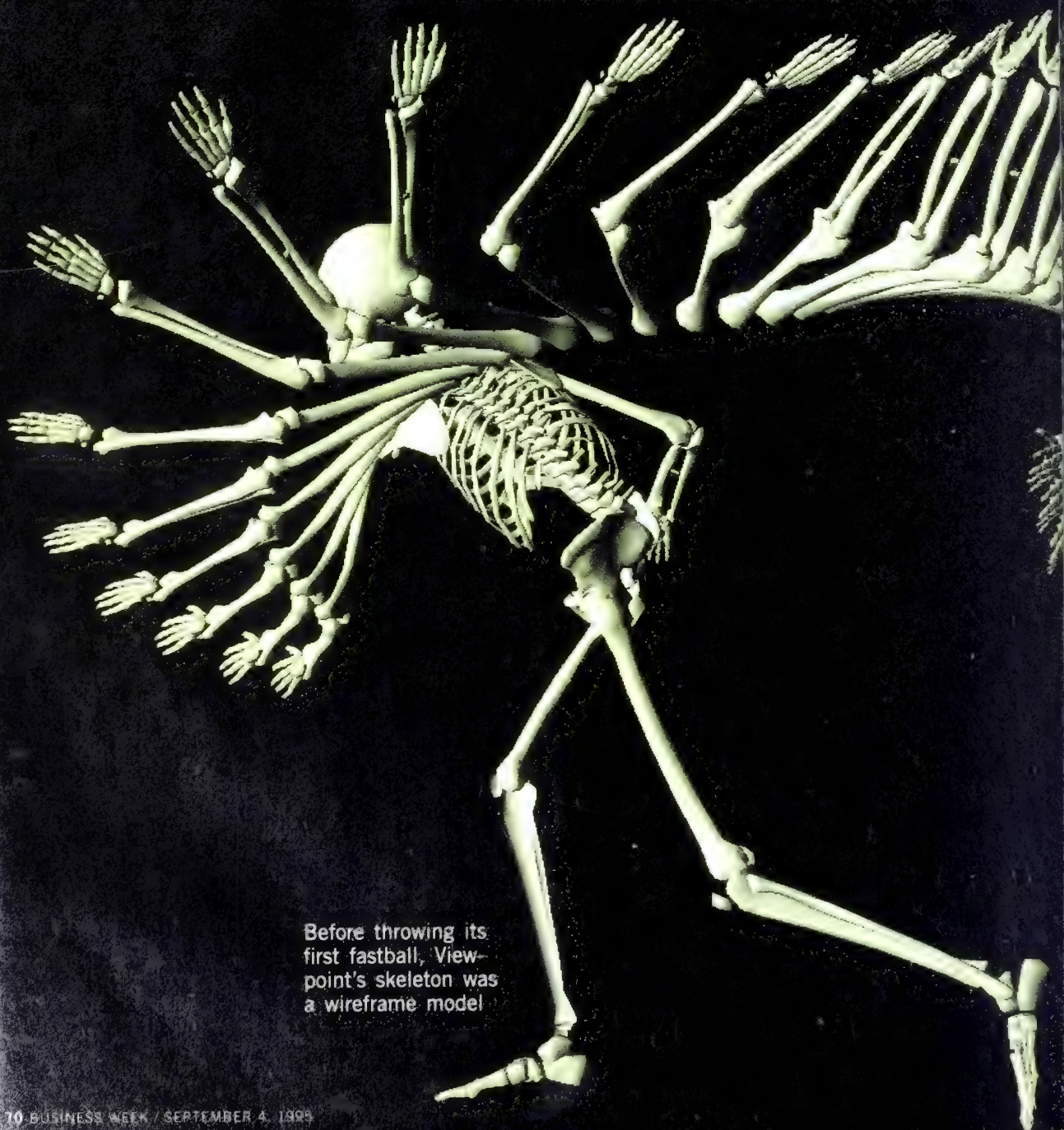
even at discounters. But the price could fall as Canon puts the technology to work in more products. New 35mm cameras, the QD series, are also due this year, and Canon sees a future for eye control in TVs and other consumer-electronics gear. "The way we'll interact with home-entertainment systems is going to be revolutionized," says Michael Zorich, technical coordinator for Canon USA Inc.



Cover Story

# 3-D COMPUTING

From medicine to war games, it's a whole new dimension



Before throwing its first fastball, Viewpoint's skeleton was a wireframe model



**R**ed troops poured across the Czech border last November, trying to capture Germany. In the counterattack, U.S. Air Force Captain Reid D. Reasor flew an F-16 out of Ramstein Air Force Base, dropping cluster bombs on bridge-  
 unkers, and Red regiments. "You got sweat-  
 ing up on your forehead," he recalls. "You  
 hear anxiety in your wingman's voice when  
 got separated."

etty exciting—for a battle that never hap-  
 ed. Reasor spent the whole time inside a 3-D  
 simulator in Mesa, Ariz. As he looked out  
 canopy" of his F-16, computers worked furi-  
 to generate the passing view of European  
 s, hills, and towns. The Army-led exercise  
 ected more than 300 sites, ranging from sub-  
 marine simulators in Newport, R.I., to infantry  
 simulators in Grafenwöhr, Germany.

The key to the biggest military simula-  
 tion ever was 3-D computing. Simula-  
 tions in three dimensions are a  
 cheap, safe supplement to conven-  
 tional exercises in a time of bud-  
 get austerity. The Defense Dept.  
 plans an even larger video war  
 game for 1997.

You don't have to work at  
 the Pentagon to appreciate  
 3-D computing. It's pervading  
 the civilian realm as well. Just  
 a few of the fields expanding  
 their horizons through 3-D vi-  
 sion: medicine, oil exploration,  
 product design, and architec-  
 ture—not to mention video  
 games, advertising, and movies.

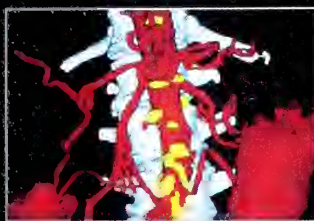
While there's no good estimate of  
 the overall 3-D market size, just look  
 at Silicon Graphics Inc. SGI, the pre-  
 mier maker of 3-D computer workstations,  
 more than tripled its revenue since 1991, to  
 billion in the year ended June 30.

ple who want to try 3-D out for themselves  
 go no further than the local toy store or  
 utor dealer. Nintendo, Sega Enterprises, Sony,  
 others are relying on dazzling 3-D effects to  
 late sales of a new generation of high-pow-  
 er game machines. And 3-D games are coming to  
 ome personal computer as well, thanks to 3-D  
 ics boards from the likes of Creative Technol-  
 ogy, 3Dfx Interactive, and NVIDIA.

ay's 3-D is a new variation on a familiar

## A NEW WAY OF SEEING

*The possibilities of 3-D, still in its infancy, are just beginning to take shape. But it's already turning up in a wide range of applications*

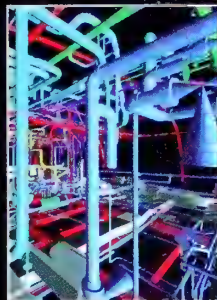


▼ **MEDICINE** Yellow blobs in a CAT scan image from Elscint represent calcifications on the aorta, which carries blood from the heart.

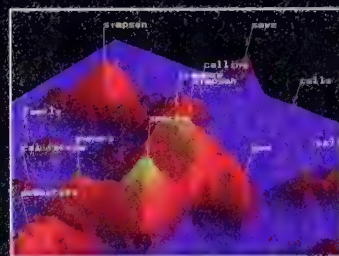
▼ **MOVIES/ADVERTISING** Industrial Light & Magic created 43 minutes of 3-D computer animation for *Casper*. Objects behind the ghosts are distorted, adding to the illusion.



▼ **ENGINEERING** Software from Intergraph shows the pipes beneath a ship's deck. If the ship's design changes, the piping routes are automatically updated.



▲ **SCIENCE** A red-and-yellow enzyme surrounds and snips a blue double helix of DNA in a model from calculations by the University of Pittsburgh's John Rosenberg.



▼ **DATA VISUALIZATION** Themescape software from Pacific Northwest Laboratory highlights connections between documents by graphing the frequency of overlap between words used.



▲ **GAMES** Players maneuver Egghead Shred by wearing sensors and making skiing motions. Dallas-based Paradigm Simulations created the game as an offshoot of defense work.



▼ **MILITARY** Twelve video images are projected inward onto a faceted dome in a new generation of cheaper, more lifelike flight simulators.



theme: ever more powerful and cheaper computers. The fan-fold paper printouts of yesteryear gave way to screens with monochrome text, followed by windowing software and simple graphics. Now, the windows are being thrown open. "3-D was always seen as a very specialized, high-cost option, like an expensive spice from China. That day is passing fast," says Dan Mapes, president of SynergyLabs, based in San Francisco, which created special effects for the new science-fiction movie *Virtuosity*. Mapes

## Cover Story

does all his effects on a network of Pentium-based PCs. Says Mapes: "We think of 3-D as simply the highest-quality way of transmitting information from one mind to another."

That's exactly why 3-D computing is so important. The brain absorbs three-dimensional information like a sponge: We've been doing it since birth. Italian painters realized that as long ago as the 15th century, when they added perspective to their paintings, aided by the geometrical insights of Florentine architect Filippo Brunelleschi. He, in turn, had simply rediscovered the classical Romans' "vanishing point"—that far-away spot in a scene at which all parallel lines seem to converge. Today, computers make it possible to step inside those perspective images and look around—say, wander around a virtual piazza and look back at the way you came in. Says Edward R. McCracken, Silicon Graphics' chairman and ceo: "Someday, all computers will be a window into three-dimensional space."

**SMOOTH SAILING.** 3-D computing isn't limited to virtual reality, whose devotees dress up in goggles and gloves to immerse themselves in an artificial environment. Most people who do 3-D computing aren't interested in total immersion—just added insight.

These are early days for 3-D. Even the fastest workstations require hours to render a single complex, high-quality image using 3-D tools—say, one frame of an animated movie. But that limitation is a good sign: If people use 3-D now, despite the inconvenience, imagine how much they'll use it when computers are vastly more powerful in 5 or 10 years.

Look how they're using it already. New Zealand sailed off with the Americas Cup this year with the help of a "digital wind tunnel"—a Silicon Graphics workstation next to the docks in San Diego that allowed its team to analyze

nearly 10,000 design variations in two months. In Japan, contractors mounted twin camera "eyes" on unmanned dozers last year, producing 3-D displays that let them remotely control the earth movers as they cleared land around Unzen Fugendake Mountain volcano. In the ultimate confirmation of its hipness, 3-D made its debut this year on World Wide Web. Instead of pages, people are building "rooms" occupied by 3-D objects—finally adding spaciousness to cyberspace.

The high sales volumes generated by video-game technology are driving down the price of 3-D equipment, and this summer's new 3-D products for home computers should accelerate the trend. These accelerator chips cost PC and board makers \$30 to \$40 apiece, one-fifth the price of their cheapest processors, says Jon Peddie Associates of Tiburon, Calif. There's still a market for the \$150-and-up chips—mainly in design, engineering, where geometric accuracy is paramount. As chips are becoming widely available. While giants such as Digital Equipment Corp. make them in-house, smaller designers hire any of several companies for fabrication.

Plunging prices will, in turn, expand the ways business can speed analysis and design to lower costs. Voith Hydro of York, Pa., uses 3-D computational fluid dynamics software in place of scale models to test the efficiency of small turbines that it sells to hydroelectric power plants. That substitution is a huge savings, since physical models cost \$500,000 apiece to build and test. The software isn't accurate enough yet to supplant models for big hydropower turbines, but it helps engineers build models that require fewer costly tweaks, says Richard A. Fisher Jr., vice-president for technology. 3-D software also produces ideas for better designs—crucial, Fisher says, since a 0.1% efficiency gain can be worth \$1 million to a customer.

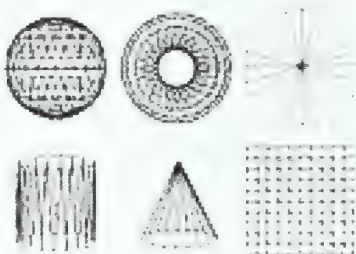
For scientists, the appeal of 3-D is the stimulation it provides for their imaginations. James Watson and Francis Crick tinkered with balls and sticks to figure out the helical structure of DNA. With computers, the toying is orders of magnitude more sophisticated. A good example is X-ray crystallography, a procedure for figuring out the placement of atoms in large molecules. Computers can make a rough guess based on the pattern made by the rays deflected off a crystalline molecule. But to get the positioning exactly right, scientists like to use a very special computer: the visual cortex.

## FLIGHT OF THE SYNTHETIC BUMBLEBEE

Here's how graphic artist Alan Henry built and flew a bee, using a Commodore Amiga computer and Imagine software from Impulse Inc.

WARTER GROUP PRESS, 1994

**1** Henry picks some building blocks, known as wireframes, which are made from tiny triangles



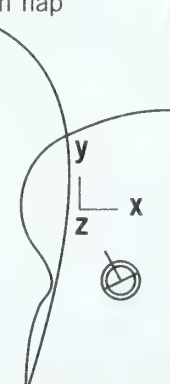
**3** Then he assembles the parts, including joints so the wings can flap



**2** He reshapes the building blocks into bee parts



**4** He sets an overhead view "flight plan" for the bee and decides where the flight will be viewed from (camera lower right)





It is so new that  
any who could  
benefit from it  
aren't. Most  
architects still  
prefer blueprints  
and cardboard

# TEXT: ULTRAREALISTIC IMAGES MAKING THEIR WAY TO THE PC

own brains. Wearing virtual-real-  
goggles and gloves, they go "inside"  
a molecule model and rearrange  
atoms by hand until the model fits  
data.

Surgeons like 3-D for similar reasons.  
In the 1930s, radiologists created 3-D  
images by crossing their eyes as they  
looked at two offset X-rays of the same  
object. Now, computers do the job for  
them, using data not only from X-rays  
but also from magnetic resonance imag-  
ing and positron emission tomography.

**BRIEFCASE HIT.** 3-D is so newly prac-  
tical that many people who could bene-  
fit from it still aren't. Most architects  
prefer to deal with 2-D blueprints and cardboard mock-  
ups, arguing that computers spoil the design process. A few  
are catching on, though. Seattle-based Callison Architecture  
uses 3-D not only for design but also for videotaped  
presentations that give such clients as Boeing, Microsoft, and  
the U.S. Navy a feel for what a new building will be like.  
James P. Rothwell, a Callison principal: "Clients love to  
watch these videos around. They become a briefcase hit."  
Now applications are heating up the battle for supremacy



bringing the bee alive by choosing its colors, texture,  
liveliness, and transparency

in 3-D space. Microsoft is making 3-D a priority. Last year, it  
bought Montreal-based SoftImage, one of the main suppliers  
of software for high-end special effects in movies and TV  
commercials. While SoftImage currently runs on Silicon  
Graphics machines, Microsoft is making it run on PCs that use  
the Windows NT operating system as well. Microsoft has  
also snagged a small British company called RenderMorph-  
ics, giving it what is likely to become the programmer's  
standard for creating PC-based video games.

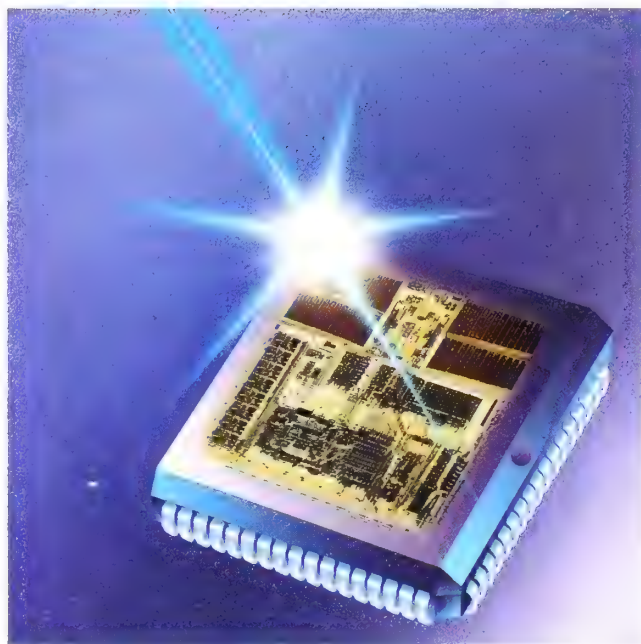
Quietly, Microsoft Chairman William H. Gates III has as-  
sembled what University of Utah computer scientist Richard  
F. Riesenfeld calls "the largest collection of graphics talent un-  
der one roof in the world." James T. Kajiya, hired from the  
California Institute of Technology last year, is working on a  
new standard for fast, cheap 3-D software and hardware  
aimed at consumers. Another hire, Alvy Ray Smith, co-  
founder of computer animator Pixar Corp., says he has want-  
ed for years to pull together sound, pictures, and animation  
into one easy-to-use package. "Nobody was big enough to pull  
it off," he says. "I think Microsoft might be."

Besides Microsoft, giants taking aim at the high end of 3-D  
computing include Sun Microsystems, king of the Internet;  
Hewlett-Packard, with new graphics accelerators; DEC; and  
IBM, which is encouraging Hollywood animators to rent pro-  
cessing time on its giant SP2 supercomputer in Maui, Hawaii.  
**REARGUARD ACTION.** For now, Mountain View (Calif.)-based  
Silicon Graphics is raking in money and riding high. Taking  
advantage of its lofty share price, SGI used \$500 million in  
stock last February to snap up two premier software compa-  
nies, Alias Research Inc. and Wavefront Technologies Inc. In  
May, it agreed to develop a computer animation system joint-  
ly with DreamWorks SKG, the "Dream Team" of Steven Spiel-  
berg, Jeffrey Katzenberg, and David Geffen.

Still, Silicon Graphics feels the heat. Its acquisition of Alias  
and Wavefront appears less a bold move than a rearguard ac-

TOP: COURTESY OF VIEWPOINT DATA; BEE: COURTESY OF VIEWPOINT DATA





*Always at the forefront of technology, SGS-THOMSON has scored many notable firsts. The chip shown here, for example, is the world's first commercially available microcomputer with on-chip power stages. It's devices like this that keep the electronics industry moving forward and SGS-THOMSON up there with the leaders.*



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*Service and Technology*

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tion to make sure those companies' programs don't migrate to cheaper machines, as SoftImage soon will. Avram Miller, Intel Corp.'s vice-president for corporate development, warns that Silicon Graphics could find itself stranded in a high-end niche with expensive, nonstandard hardware, as happened a decade ago to Digital Equipment Corp. "This is DEC in 1985," Miller argues. "Once this thing starts coming apart, it comes apart pretty quick."

## Cover Story

that happen. He's trying to get as many manufacturers as possible to adopt the company's chip design, called MIPS. Two high-volume wins: Sony's PlayStation uses a MIPS design from LSI Logic Corp., and SGI designed a MIPS-based chip for Nintendo's Ultra 64. McCracken isn't worried about Microsoft for the next four to six years, which he says is as far out as he can project. "Let Microsoft and their partners sell a few million units," he says. "More people will know how to program in 3-D."

He has a point. In these early days of the 3-D boom, demand is growing at such a rapid pace that plenty of suppliers should be able to make a buck off the third dimension.

Plenty already are. Autodesk Inc., the maker of computer-aided design software for PCs, has become a major force by opening up its 3D Studio entertainment software to makers of "plug-ins"—software modules for special effects for movies and commercials such as sepia tones, fog, or bubbles. MultiGen Inc. specializes in extra-fast rendering of 3-D for video games and flight simulators—where there's no time to create each frame in lifelike detail. Its software draws the buildings that people "fly" over on a carpet in Walt Disney Co.'s knock-out new Aladdin attraction at Epcot Center.

**QUANTUM LEAP.** 3-D is generating new business opportunities for smart companies such as Viewpoint DataLabs Inc. in Orem, Utah. Viewpoint builds everything from helicopters to body parts out of "wireframes," which look like chicken-wire sculptures and are easy to manipulate by computer. The digital prop house sells these 3-D objects to moviemakers, the military, and others. Viewpoint made the skeleton on the first page of this article and programmed it to throw a baseball by copying the arm motions of human volunteers. A moviemaker could simply dress the skeleton in cyberflesh and a baseball uniform.

The next step beyond viewing 3-D images on flat screens is stereoscopy—as in the 3-D glasses for 1950s horror movies such as *Creature from the Black Lagoon*. Stereoscopy mimics the real world, in which people gauge distance by the way their two eyes see the same object from different angles. Today's virtual-reality goggles are a quantum leap beyond the colored cellophane lenses of the 1950s. Says Linden Rhoads, president of Seattle-

**"3-D was always seen as a specialized, high-cost option, like an expensive spice. That day is passing fast"**

**GULP: A 3-D ANIMATION SHOWS THE WORKINGS OF THE DIGESTIVE SYSTEM**

Silicon Graphics CEO McCracken vows not to let

## WHO'S WHO IN THE THIRD DIMENSION

*A sample of the major players*

**SILICON GRAPHICS (SGI)** The premier maker of workstations for 3-D imagery in engineering, entertainment, and other fields. Challenged on all fronts.

**MICROSOFT (MSFT)** The software giant has pegged 3-D as a growth market; wants to seize leadership of software-writing "tools" from SGI.

**AUTODESK (ACAD)** The top maker of 3-D design software for personal computers has successfully branched into effects for movies and commercials.

**MACNEAL-SCHWENDLER (MNS)** Makes industrial-strength 3-D software for engineers that runs on machines ranging up to supercomputers. Focuses more on accurate modeling than on glitzy display.

**INDUSTRIAL LIGHT & MAGIC** Off the beaten track in Marin County, Calif., but the undisputed leader in 3-D effects for movies, with credits such as *Jurassic Park* and *Casper*.

**EVANS & SUTHERLAND (ESCC)** The original 3-company started by building flight simulators. Now it also sells 3-D accelerator chips to the likes of Sun Microsystems, Hewlett-Packard, and IBM.

**SEGA (SEGN)** Leaped ahead of Nintendo with the Japanese debut of its 3-D game machine, Saturn. But Nintendo, Sony, Atari, and 3DO are in the race.

based goggles maker Virtual i-O: "Stereoscopy is just more compelling—the same as we like talking films more than silent ones and color films more than black-and-white.

Goggles are a bit cumbersome, though, and certain po-

designed ones can cause side effects ranging from headaches to disorientation. That's why inventors around the world are racing to develop displays that produce two different eye views with glasses. Australian inventor Donald Martin has one involving vertical bars that whiz by in front of the screen. Last year the U.S. Navy revealed that it can create 3-D images by firing 40,000 laser beams into something that looks like a round transparent washing machine, complete with a spiral-shaped agitator. Sharp Industries of Europe Ltd. has built a prototype 3-D display that remotely senses the viewer's head movements and responds by moving lenses to change the scene presented to each eye.

Holography is advancing as a 3-D medium, too, and not just as the pigeon on your credit card. Holograms can now be made in full, natural color, thanks to a 1992 breakthrough by Hans I. Bjelkheden. In his new job as vice-president of research and development at AmeriPropylaea Corp. in Birmingham, Mi-





wedish researcher is working to make his full-color horns bigger, brighter, and viewable from more angles. Day's 3-D is miles beyond what was possible in the past, when the most sophisticated computer graphics in the world were being done in Salt Lake City. The University of Utah became a mecca thanks to faculty members David Evans and Ivan E. Sutherland. Those two later founded Evans & Sutherland Computer Corp., which remains No. 1 in the world for flight simulators. Utah alumni include Jim Clark, founder of Silicon Graphics; John E. Warnock, founder of Evans & Sutherland Systems; Alan Kay, principal scientist of Apple Computer; Alan Ashton, founder of WordPerfect; and Ed Catmull, who co-founded Pixar with Alvy Ray Smith.

**LOVE.** Computer memory in those early days was insufficient to hold animation, so programmers stored images directly onto film. To capture a frame, they would keep the camera's shutter open as the computer generated the image, frame by frame. Since the screen was monochrome, they had to do multiple passes with filters to get color images. That took true patience. Henry C. Christiansen, a Brigham Young University professor who did his research at Utah, says they borrowed the audio of the Mormon Church to make "movies" of such quality as the vibration and flutter of experimental NASA aircraft. Says Christiansen: "I used to work all night, until my arms crashed."

Creating good 3-D still is no snap, but lots more tools are being added. Existing blocks exist. If photorealism is the object, artists create reflections by letting the computer calculate the path of light rays. They can also add "radiosity," so a hand on a bright yellow car will pick up a yellow glow. If speed is the object, forget computation-intensive tricks like ray-tracing. The processor in a shoot-'em-up video game is busy trying to redraw tanks and missiles 30 to 60 times a second. Video-game programmers try to retain a respectable degree of realism while staying within the all-important "polygon budget"—the maximum number of geometric shapes that the processor can draw per second. One shortcut is to compensate for the lack of detail with "texture maps"—2-D pictures that are pasted onto the sides of polygons.

**SOFT WHIZ  
IS WORKING  
FASTER 3-D  
CONSUMERS**

As people embrace 3-D, they must also understand its limitations. Computer simulations, no matter how seemingly accurate, are not replicas of real-



**VIRTUAL I-O CEO  
RHODES SEES  
THE FUTURE IN  
STEREOSCOPY**

ity. Case in point: When Boeing Co. engineers probed the 1992 crash of an El Al Israel Airlines 747 cargo flight that slammed into low-income housing in the Netherlands, killing 43 people, they discovered that their finite element analysis stress simulation had not been detailed enough. It had missed several weak points in the design of a "fuse pin" that held the engines to the wings. One fuse pin broke, and the plane went into a fatal dive. A similar simulation flaw led to the sinking of a huge oil platform in a Norwegian fjord in 1991.

Sometimes, 3-D pictures end up just being confusing. Pacific Northwest Laboratories in Richland, Wash., found that out when researchers wrote a data-visualization program called Galaxies. Each document was characterized by a point, or "star." You could tell how similar documents were by how closely the stars clustered on a 2-D chart. The system worked fine until the lab added another variable. When users put on VR goggles to explore the proximity of stars in three dimensions, they became disoriented—"lost in space," says staff scientist James A. Wise. The lab has had better luck with another program, Theme-scapes, that portrays data as hills and valleys.

Like no other field of computing, 3-D hits people in the gut. Just ask the kids from Orville Wright Magnet School in Los Angeles, who got a preview of Nintendo's 3-D Virtual Boy at a trade show last May. Their one complaint was that the \$180 machine only displays red on black. Wrote middle-schooler Aja Thrasher: "It would really be Da Bomb if you are able to make this in color." When it comes to 3-D, everybody's got something to say.

*By Peter Coy in New York, with Robert D. Hof in Mountain View, Calif.*



PHOTOGRAPHS BY ALEX KENNEDY





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# UNISYS



# BALANCE SHEETS THAT GET WELL SOON

Columbia/HCA's hospitals sure are lean. Are they mean?

**I**t was quick—and slick. In April, South Miami Hospital was about to merge with nearby Baptist Health Systems, when Columbia-HCA Healthcare Corp. swooped in with a counteroffer. The huge for-profit hospital chain had a proposal hand-delivered to all 224 members of South Miami's foundation. It matched Baptist's offer to assume the hospital's \$70 million debt load, while kicking in \$20 million in fresh capital. Columbia even encouraged its doctors to call their South Miami colleagues to extol the virtues of joining up.

But instead of tempting them, the aggressive salesmanship alienated foundation members, who feared the community would lose control to profit-driven managers at Columbia headquarters, 900 miles away in Nashville. South Miami chose Baptist. "These were not the sort of people we wanted to do business with in the long term," says Dr. Melvin A. Mackler, chairman of South Miami's board.

Mackler's misgivings aren't unique. By bringing to health care the sort of hard-nosed dealmaking, consolidating, and cost-cutting tactics that have made other U.S. industries lean, agile, and profitable, Columbia's chief executive, Richard L. Scott, has created a \$15 billion juggernaut in just eight short years. And the sort of resistance Columbia met in Miami is hardly likely to slow the company's growth. But the chain's brisk ascendancy has ignited a debate in the health-care industry about its tactics, ambitions, and style of operations.

**"ARROGANT BULLIES."** Some communities are in an uproar over Columbia's purchase of local nonprofit hospitals, some over its attempts to cut back money-losing services. On May 16, Florida regulators revoked Columbia's license to operate a 50-bed hospital in Destin after locals protested Columbia's sudden decision to curtail many patient services at the loss-ridden facility. The chain argued that there were two other hospitals just 10 miles away and that the hospital never filled more than 14 of its beds. Columbia is appealing the decision.

Rival hospitals are fuming over Columbia's hardball tactics as it tries to wrestle away market share. After Northwest Medical Center in Houston turned down an offer from Columbia, the chain laid out plans to build a new 100-bed hospital—right across the street. Northwest, which is filling only 50% of its 500 beds, says there's no need for another

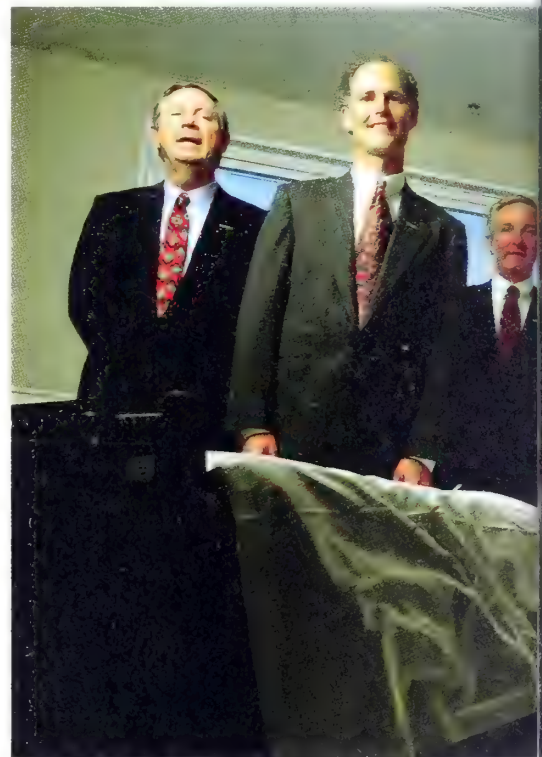
Columbia's growth is yielding huge returns. One analyst sees profits climbing 28% this year, to \$1.3 billion. And operating margins could hit 21%

hospital. "They're arrogant bullies," says Northwest CEO J. Barry Shevchuk. Columbia says it needs a hospital to complete its coverage of Houston.

The most worrisome question raised by Columbia's expansion is whether its bottom-line brand of health care will end up being good for patients. Critics—including some Columbia hospital staffers—are especially concerned about the company's quest to drive down costs and boost margins. At some Columbia hospitals, the company is replacing nurses with lower-paid staffers to handle such

mundane chores as taking vital signs. At the chain's Columbia East Hospital in El Paso, doctors opposed nursing in the maternity ward. "We felt we were getting to the point where patient care was compromised," says Dr. Joel Drix, chief of obstetrics at Columbia. Columbia backed down after meeting with doctors. It says such discussions are typical of all hospitals.

Nonprofits also complain that Columbia cherry-picks profitable patients, leaving them to handle the bulk of indigent cases (page 84). Critics charge the practice is encouraged by a program that gives physicians part-ownership of some facilities. A 1993 study by Florida's Agency for Health Care Administration warned of "a possibility of cream skimming" by examining 2,238 Medicare cases handled by doctors who had privileges at Columbia's Victoria Hospital as well as at other for-profit hospitals in Miami. The report



**EXPANSION TEAM:** Columbia/HCA's McWhorter, Scott, and Frist

cluded that lucrative cases were more likely to be admitted to Victoria, while less profitable ones were sent elsewhere.

Columbia denies that its doctors screen patients for profitability. The company commissioned two studies of hospital missions in Florida that found no evidence that its physicians were dumping charity cases. Furthermore, Columbia says it spent \$1 billion on uncompensated care last year.



# Columbia Makes a Capital Costs

## INTEGRATION

After buying a variety of health-care facilities, it consolidates services in each market to reduce costs, pool talent, and offer a wide menu to managed-care providers.

## STAFFING

Uses less-skilled, lower-paid workers to take over many of the responsibilities of higher-paid staffers. Reading EKGs, for example, may now be done by nurse's aides instead of registered nurses.

## CENTRAL PURCHASING

Thanks to its size, it negotiates significant price breaks with its suppliers. Company estimates it saved about \$300 million on the \$2.5 billion it spends yearly on supplies.

## INCENTIVES

In some markets, it offers physicians equity investments in local Columbia networks to encourage doctors to take a more active role in improving operations.

be sure, a company the size of Columbia is bound to draw critics. With hospitals and more than 100 outpatient surgery centers, as well as home care, it's already the biggest private health-care provider in the nation. And to surprise that Columbia's competitive style would raise hackles in the sheltered health-care industry. "It's part of being a large company in an industry going through significant change and being perceived as a compa-

dard method yet for measuring how patients fare in an increasingly cost-conscious environment. Meanwhile, some hospital administrators warn that the unprecedented flurry of dealmaking in the industry is getting out of hand.

Already, Columbia is feeling the heat of closer legal scrutiny of some of its deals. On June 21, a U.S. grand jury began investigating whether the former head of Tampa General Hospital, David Bussone, made bad business decisions, such as

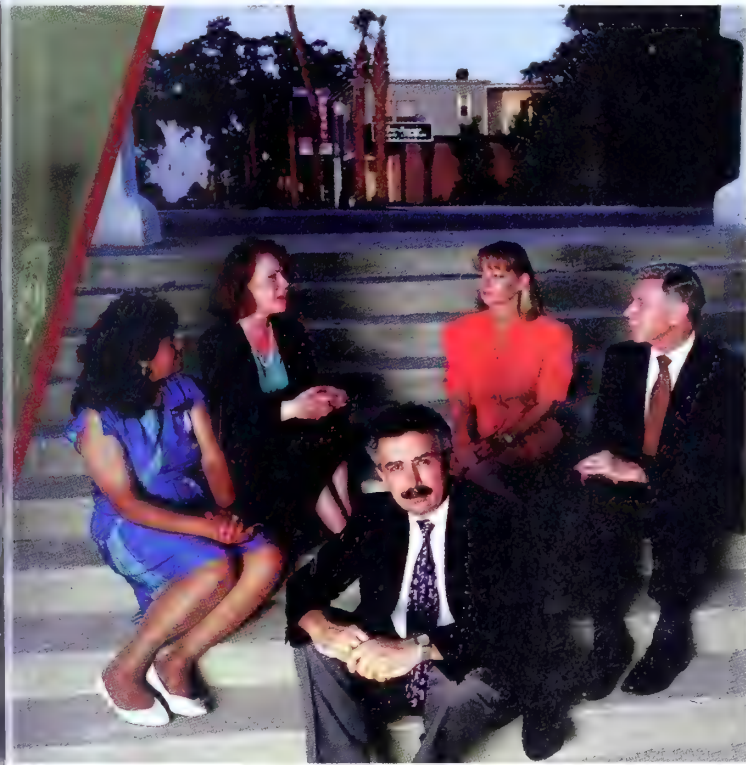
doughnut shops he owned while attending the University of Missouri. A lawyer by training, he started out in Dallas specializing in small health-care company buyouts. There, Scott met investor Richard Rainwater. On the day of the market crash in October, 1987, they each kicked in \$125,000 to start Columbia.

**ONWARD.** Columbia has been growing ever since. Having snapped up Galen Health Care Inc. in 1993, HCA/Hospital Corp. of America in 1994 and Health-

Trust Inc. earlier this year, Columbia is three times the size of its closest for-profit competitor, Tenet Healthcare Corp., based in Santa Monica, Calif. And it's expanding into new regions. Vice-Chairman Thomas F. Frist Jr., the former head of HCA, says Columbia will spend \$1 billion in the next year or so on ventures in Massachusetts, a state dominated by nonprofit hospitals.

Columbia's insatiable quest for growth is producing huge returns for shareholders. Analyst Carl Sherman of Dillon, Read & Co. estimates that profits from continuing operations may climb 28% this

Critics say  
doctors' equity  
encourages  
them to shunt  
the poor away  
from Colum-  
bia's hospitals,  
and nonprofits  
say they see  
more indigent  
cases when  
Columbia  
comes to town



**IN MY BACKYARD:** Tarpon Springs City Manager Yatikiotis led efforts in thwarting a Columbia buyout.

making change happen," says Scott. "It is Columbia unique in provoking controversy in health care. Throughout the industry, market forces are filling the vacuum created by Washington's failed effort to craft meaningful reform to deliver care and cut costs. Health-care experts agree that hospitals might not be able to find an acceptable balance between profitability and mission. But there is no stan-

buying a money-losing psychiatric facility, to lower the value of the hospital and make it easier for Columbia to buy. Bussone later went to work for Columbia. Both Columbia and Bussone deny wrongdoing, and the deal was never concluded. Bussone's lawyer says he applied for a job with Columbia only after he was asked to resign by Tampa General.

Scott, 42, would seem an unlikely champion of health-care reform. Eight years ago, he knew nothing about hospital management. In fact, his only management experience was running two

year, to \$1.3 billion, as revenues rise 21%, to \$17.6 billion. Thanks to lower costs, Columbia's operating margins may reach 21.2% this year, compared with 18.6% three years ago.

Few question Columbia's ability to wring efficiencies from the fragmented hospital industry, often by reducing capacity. When Columbia came to El Paso in 1988, it paid \$60 million for two ailing hospitals and has since spent \$140 million to upgrade them. Then Columbia shelled out about \$20 million to buy Landmark Medical Center and shut it down. By re-



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ducing the number of beds in El Paso by 16%, Columbia has helped boost occupancy at other hospitals, including its own. "El Paso is better off today than it was before Columbia came in," says David Buchmueller, CEO of rival Providence Memorial Hospital.

Meanwhile, its awesome clout with suppliers helps it to cut expenses. For example, the chain hopes to cut costs for orthopedic implants from \$100 million to \$55 million a year. Altogether, Samuel A. Greco, Columbia's senior vice-president of financial operations, estimates the company saved roughly \$300 million on the \$2.5 billion it spent on supplies last year.

Columbia's economic impact is being

felt industrywide. Thanks largely to Columbia, Amy K. Knapp, executive director of Prudential Health Care System of South Florida, reckons that managed-care companies in her region are paying hospitals 10% less than they were two years ago. "It's very clear Columbia's presence in this marketplace has stimulated the hospitals to be much more competitive than they otherwise would be," she says.

Critics charge, however, that some of that newfound competitiveness comes at the expense of nonprofit hospitals and the indigent patients they serve. In many areas where Columbia operates, nonprofit hospitals complain that they have to handle a rising share of nonemergency,

charity patients. At Kendall Regency Hospital near Miami, acquired by Columbia in 1991, uncompensated and charity care dropped from \$10.1 million in 1992 to \$8.6 million from 1992 to 1994, while nearby Baptist's load rose from \$10 million to \$19.7 million.

**CONFLICT?** Nonprofits charge that Columbia's physician-ownership program encourages doctors to shunt charity cases away from its hospitals. In some markets, Columbia groups its assets in a limited partnership and sells as much as 20% to its local physicians. And it creates an inherent conflict of interest, says Fred Hirt, president and CEO of the nonprofit Mount Sinai Hospital in Miami, a Columbia competitor. "We have a strong belief that it is not right for a person who practices in a facility to have a vested interest in ownership," he says. Columbia denies that the program creates any conflicts and says only 2.5% of its assets are owned by such interests. Columbia Chairman R. Clay McWhorter also points out that many nonprofits have similar programs.

As for any misgivings about quality, Scott insists Columbia's care is superb. He points to 58 Columbia hospitals that have received accreditation with commendation from the Joint Commission on Accreditation of Healthcare Organizations, which grades 11,000 health facilities. Only 4% of U.S. hospitals won that rating. And Columbia is spending \$150 million to upgrade a computer system that tracks how its patients do. "We're more focused on being cost-effective and quality-oriented than any company out there," Scott says.

Still, Columbia is starting to hit speed bumps: In April, Tarpon Springs, Fla., led by City Manager Costas Yatikiotis, thwarted a deal by Columbia to acquire the local community hospital in part over concerns that Columbia would skimp on charity care. In Massachusetts, Attorney General Robert Healy would call a public hearing on Columbia's proposed joint venture with MetroWest Health Inc., a Framingham hospital. Among the issues: safeguarding the accessibility and affordability of care.

Not that there's much chance Columbia's expansion will slow significantly. With so many hospitals facing tight budgets, there's no shortage of would-be partners. "People are coming to us," Scott says. After all, if there's one thing Columbia knows how to cure, it's a tight balance sheet.

*By Zachary Schiller in Nashville, with Gail DeGeorge in Miami, Stephen Anderson Forest in San Antonio, and Eric Schine in El Paso, and bureau rep-*

## MEANWHILE, A PUBLIC HOSPITAL STRUGGLES TO SERVE

**F**or 38 years, E. V. Thomason Memorial Hospital has been a fixture in El Paso, Tex., the dusty border city where Columbia/HCA Healthcare Corp. got started in 1988. Its emergency room, immunization program, and outlying clinics have been among the few sources of quality health care for El Paso's poor—about 30% of the city's population of 650,000. Now, the 289-bed county hospital is struggling. Thomason is expected to treat 100,000 emergency-room patients this year—triple the volume of the mid-1980s.

And though the cost of its charity workload is expected to climb 16% this year, to \$44 million, its annual federal funding has plunged 58% since 1991, to \$24 million.

At the same time, Thomason finds itself waging an unlikely battle for revenue-producing Medicaid patients with its for-profit rivals in El Paso, Columbia/HCA and Tenet Healthcare Corp. Since January, the number of Thomason Medicaid patients has slipped by 6%. "We're getting squeezed by the two giants," says Pete Duarte, chief executive of Thomason.

The squeeze is particularly painful because Thomason has long used Medicaid revenues to subsidize its charity care. The federal government typically reimburses hospitals up to 80% of the bill for Medicaid patients, and Medicaid money usually accounts



**EMERGENCY:** El Paso's Thomason Hospital

for a critical 40% of the hospital's operating revenues.

But Columbia and Tenet, each of which operates two hospitals in El Paso, are aggressively wooing Medicaid patients—especially lucrative maternity cases. With its revenues expected to drop 10% this year, to \$89 million, Thomason may have to curtail many of its public-health services, including participation in the county's aggressive immunization program. And county health officials worry that Columbia and Tenet won't step up to help fill the gap. But they haven't received any promises. Says Dr. Laurance N. Nickey, director of the El Paso Health & Environmental District: "When it comes up that the people we treat have no insurance, the conversation trails off."

*By Eric Schine in El Paso*



COMMENTARY

By Howard Gleckman

# GOP MAGIC: TRIMMED BUDGET, BRIMMING TROUGH

When they were swept into office last November, congressional Republicans duly vowed to balance the budget and remake government by scrapping residues of obsolete or wasteful federal programs, ending industrial policy, and turning over a variety of government duties to the private sector. Instead, when GOP lawmakers return to Washington in September, you'll be putting the finishing touches on a revolution with a decidedly all right. They have trimmed much, killed little. They've slashed a handful of federal research programs embraced by President Clinton but untouched scores of other business subsidies. They've hacked away housing assistance for the poor, enforcement of environmental laws but larded the Pentagon budget with projects that even the generals don't want. Says moderate Democratic Progressive Policy Institute vice-President Robert J. Shapiro: "They have largely left untouched a catalog of spending for powerful industries."

**ENTRAPMENT.** To be sure, the GOP deserves credit for engineering the long-needed spending cuts and making deficit reduction a top priority. But by trashing Democratic constituencies while protecting their own, the Republicans are undercutting their credibility. And it could cost them dearly over the next few months as they try to sell skeptical voters on cuts in Medicare benefits. Their argument will be based, in part, on claims that everyone must get their fair share to help balance the budget. Yet a promised \$245 billion tax cut most beneficial to businesses and the well-to-do already makes that argument seem hollow. And with fat-cat corporate contributors dodging the spending axe, GOP pleas for shared patriotic sacrifice verge on the ridiculous. So far, Congress has only partially



**STEALTH PORK:** Critics say B2s deliver a payload of lard

completed work on the 13 money bills that set spending levels for much of what Washington does—from law enforcement to export subsidies. And big chunks of government, including entitlements such as Medicaid and welfare, as well as Medicare, must be tackled separately. But already, the GOP has sent a strong signal about just where it wants to take government.

Defense spending is a good example. In an era of spending restraint, the Pentagon would get about \$5 billion more in fiscal 1996 than it did this year. Why? The Senate would build four Aegis cruisers, two more than the Navy wants. Not coincidentally, the ships would be built in Maine and Mississippi, home states of the chairman of the armed services' sea power subcommittee, William S. Cohen (R-Me.), and Majority Whip Trent Lott (R-Miss.). The House would spend \$540 million to maintain the production line for the B2 bomber even though the Air Force says it doesn't need more of the costly

planes. Meanwhile, both houses would throw a pile of cash at a new Star Wars antimissile defense system.

Backers of the project insist it would protect the U.S. from nuclear attack by rogue nations such as North Korea. Critics, however, see only fiscal cholesterol. "Calling the funding pork is unfair to pigs," fumes Senator Byron L. Dorgan (D-N.D.). "This is pure, unadulterated lard."

The Republican Party's view on corporate subsidies is a little different.

The GOP would continue to fund the Export-Import Bank and the Agriculture Dept.'s marketing promotion program—both of which shower largesse on big U.S. corporations such as Boeing Co. and Pillsbury Co. but do little for the country's small and midsize companies. Farm subsidies still haven't been cut. And despite all the promises to privatize everything from the air traffic control system to the federal agencies that provide inexpensive electric power in the West and South, little would actually be sold off.

**WRONG REFRAIN.** However, other business aid—particularly that embraced by President Clinton and labeled industrial policy—is a goner. The House GOP would eliminate funding for the Advanced Technology Program and slash spending for the High Performance Computing & Communications Initiative—two high-profile federal programs that promote high-tech research. Complains National Economic Council Chairman Laura D'Andrea Tyson: "There's a targeting of the Clinton investment agenda."

Republican apologists insist there's nothing wrong with helping supporters while punishing the opposition. That, they say, is the way it has always been done in Washington. And that's exactly the problem.

**GOP pleas for shared sacrifice sound like someone has a bridge for sale**

Senior Correspondent Gleckman covers fiscal policy from Washington.



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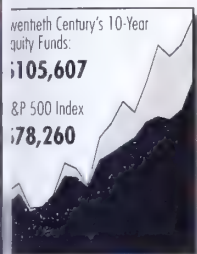
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that would have happened to a hypothetical \$20,000 investment made equally on 6/30/85 among Twentieth Century equity funds that have been in existence for at least 10 years: Vista, Select, Growth, Ultra, and Giftrust, compared to the same investment in the stocks that comprise the S&P 500 during the 10-year period ending 6/30/95. Past performance does not guarantee future results.

existence for at least 10 years substantially outperformed the S&P 500 over the 10-year period ending 6/30/95. In fact, the Twentieth Century investment would have earned **35%** more than the S&P 500.

And now we'd like to add something you don't always see in mutual fund advertising: a word of caution.

It happens that some of our one-year gains, shown on the right, are fairly substantial. But we hope you won't put too much emphasis on 12-month returns, but rather on consistent long-term performance. In order to put the power of the stock market on your side, it's simply wiser to keep your focus on the long-term.

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## TWENTIETH CENTURY'S PERFORMANCE OVER TIME

Average Annual Total Returns as of 6/30/95

| Fund                        | Life of Fund               | 10-Year      | 5-Year       | 3-Year       | 1-Year       |
|-----------------------------|----------------------------|--------------|--------------|--------------|--------------|
| <b>Vista Investors</b>      | <b>13.5%</b><br>(11/25/83) | <b>16.1%</b> | <b>12.5%</b> | <b>17.9%</b> | <b>55.4%</b> |
| <b>Select Investors</b>     | <b>16.6%</b><br>(6/30/71)  | <b>12.3%</b> | <b>7.4%</b>  | <b>9.2%</b>  | <b>16.5%</b> |
| <b>Growth Investors</b>     | <b>18.5%</b><br>(6/30/71)  | <b>15.5%</b> | <b>11.2%</b> | <b>10.1%</b> | <b>22.7%</b> |
| <b>Ultra Investors</b>      | <b>17.4%</b><br>(11/02/81) | <b>19.0%</b> | <b>21.3%</b> | <b>20.1%</b> | <b>29.0%</b> |
| <b>Giftrust** Investors</b> | <b>22.3%</b><br>(11/25/83) | <b>24.3%</b> | <b>25.5%</b> | <b>39.5%</b> | <b>60.4%</b> |
| <b>S&amp;P 500 Index</b>    | —                          | <b>14.6%</b> | <b>12.1%</b> | <b>13.2%</b> | <b>26.0%</b> |

\*\* Giftrust is a unique fund designed to be given as a long-term gift to someone other than yourself or your spouse

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domestic mid-cap funds during investment periods ending 6/30/95, Lipper Analytical Services, Inc., an independent mutual fund ranking service, ranked Twentieth Century funds #22 out of 32 funds for the five-year period and #4 out of 17 funds for the 10-year period. ■ Data quoted is based on past performance and assumes reinvestment of all distributions. ■ Investment return and principal value will fluctuate, and redemption value may be more or less than original cost. ■ The S&P 500 Index is an index created by Standard & Poor's Corporation that is considered to reflect the performance of the stock market. ■ It is not an investment product available for purchase. ■ The graph is intended to show investments over time. Included in the investment blend are only Twentieth Century equity funds in existence for 10 years or more and the performance above represents only those funds. ■ All performance illustrations for Twentieth Century are shown net of fees and assume reinvestment of all distributions. P.O. Box 419200 Kansas City, MO 64141-6200 BSW © 1995 Twentieth Century Services, Inc.



# A BREAST-IMPLANT DEAL COMES DOWN TO THE WIRE

All parties have a huge stake in a single settlement, rather than thousands of jury trials



**POWER IN NUMBERS:** Plaintiff Armstrong may mount a consumer boycott

It seemed to be such a good idea a year ago. In his courtroom in Birmingham, Ala., U.S. District Judge Sam C. Pointer Jr. had given approval to the largest settlement in litigation history. In one fell swoop, a \$4.2 billion package put to rest much of a 20-year-old pandemonium associated with thousands of claims made by women who said silicone-gel breast implants had made them sick. The plaintiffs would get money for their physical and mental anguish. And implant manufacturers such as Allergan Inc., Corning Corp. and Bristol-Myers Squibb Co. would avoid a legal nightmare that threatened financial upheaval and seemingly endless courtroom brawls.

As it turns out, the class-action settlement began to crumble almost as soon as the ink from Pointer's pen had dried. Some 440,000 women, many more than expected, registered throughout the country to get a piece of the \$4.2 billion pie, either now or when they become ill in the future. About 70,000 of them appealed to qualify for immediate compensation beyond the 6,000 originally anticipated. Another 8,000 women elected to opt out of the deal altogether, choosing instead to pursue their cases in court. "It's the biggest mess you've ever seen," says Gail Armstrong, an implant recipient who serves as the consumer adviser to the global settlement.

Now, working under an Aug. 30 deadline set by the judge, plaintiffs and defendants are scrambling to rescue the package. "It's an extremely difficult problem," says Pointer, who in May sent both sides back to the drawing board. "I certainly have hopes but also serious doubts as to whether it can be worked out."

Although substantial progress has been made, BUSINESS WEEK has learned that an industrywide deal is unlikely by September. Instead, according to sources close to the negotiations, Bristol-Myers is spearheading an effort to craft a mir-

## Inconclusive science



of sorts with co-defendant Union Carbide that will lure other manufacturers. "I'm cautiously optimistic," says Stanley Chesley, one of the plaintiffs' chief negotiators. "The settlement process is still evolving, would be defendants other than Dow to chip in a total of \$3.6 billion, 2% more than their original contribution of \$2.1 billion. If the settlement, which filed for bankruptcy in May, could be persuaded to accept the deal, the package could be as much as \$7.2 billion. More cash doesn't mean more money for individual plaintiffs because there are too many of them. The current plan involves cases involving the vast majority of claimants—women with a serious health problem that can be split off from those with more debilitating conditions. Compensation, which had ranged from \$140,000 to \$1.4 million, depending on each plaintiff's medical situation, will be reduced. Moreover, defendants are going to require women to agree with a revised deal to their disputes rather than go to trial, sources say. Talks could break down as settlement deadline approaches. No agreement even exists yet. But lawyers involved in the case agree that the gamble would be to let the plan perish. "I believe the global deal is the best alternative to securing global peace in this litigation," says Kenneth R. Feinberg, Dow's point man in the negotiations. "I think we can permit the deal to stand and send hundreds of thousands of women back to court."

Not? Because most participants in the case see the stakes as just too high. To many recipients, who would otherwise wait for their cases to wind up through court, a deal offers a quick financial help. Their lawyers, who have spent millions bringing suits, want to see a return on the investment for themselves and their clients. Even as the tide has begun to turn in the defendants' favor, with new casting doubt on links between breast implants and various diseases, manufacturers remain willing to bargain. A reworked settlement would be preferable to the uncertainty of years of litigation, they say. Implant makers have had notable successes in court, but



## GEL IMPLANT

Makers have become the poster kids of tort-reform activists in Washington

## Who's on the Hook

**DOW CORNING** Formerly the largest maker and seller of silicone-gel breast implants. Dow Corning also sold materials used by other makers.

PENDING LAWSUITS/  
CLAIMS

19,000

AMOUNT PLEDGED  
TO CURRENT DEAL

\$2.02 BILLION

**BRISTOL-MYERS SQUIBB** Was the No. 2 maker and seller of silicone-gel breast implants.

10,000

\$1.15 BILLION

**BAXTER INTERNATIONAL** A division of a company purchased by Baxter in 1985 had made and sold silicone breast implants.

8,030

\$556 MILLION

**3M** Made and sold silicone-gel breast implants through McGhan Medical from 1977 to 84.

6,597

\$325 MILLION

DATA: COURT RECORDS, COMPANY FINANCIAL STATEMENTS

they have also had some painful experiences. Bristol-Myers, for one, was hit with a \$25 million verdict in 1992. "We continue to believe that resolving most of the claims through a single forum is in the best interests of all the parties involved," says a spokesperson for Baxter International Inc., one of the defendants. **SCRATCH ONE BILLION.** Baxter's eagerness for a deal shows just how much the industry craves an end to this legal fiasco: The Deerfield (Ill.)-based company hasn't been officially involved in the talks since July, when it was expelled by plaintiffs for balking at their demands. Dow Corning, too, has stayed on the sidelines. On Aug. 22, its counsel met plaintiffs' lawyers for the first time in months to initiate talks on a revised deal.

There are many factors impelling everyone toward settlement. Dow Corning, which is in danger of becoming the property of its largest creditor, breast-implant plaintiffs, says it has already spent \$1 billion defending itself. "It was Litigation Inc. that forced us into this situation," fumes Dow Corning's president,

Gary Anderson. Dow Corning's half owner, Dow Chemical Co., which is not part of the settlement talks, says it spends \$10 million a year on legal fees generated by some 3,000 breast-implant cases.

On the plaintiffs' side, too, a collapsed agreement means delay and a loss of millions. One estimate puts plaintiffs' lawyers' investment at least at \$200 million. The women at the center of the storm could end up with nothing from an unsympathetic jury.

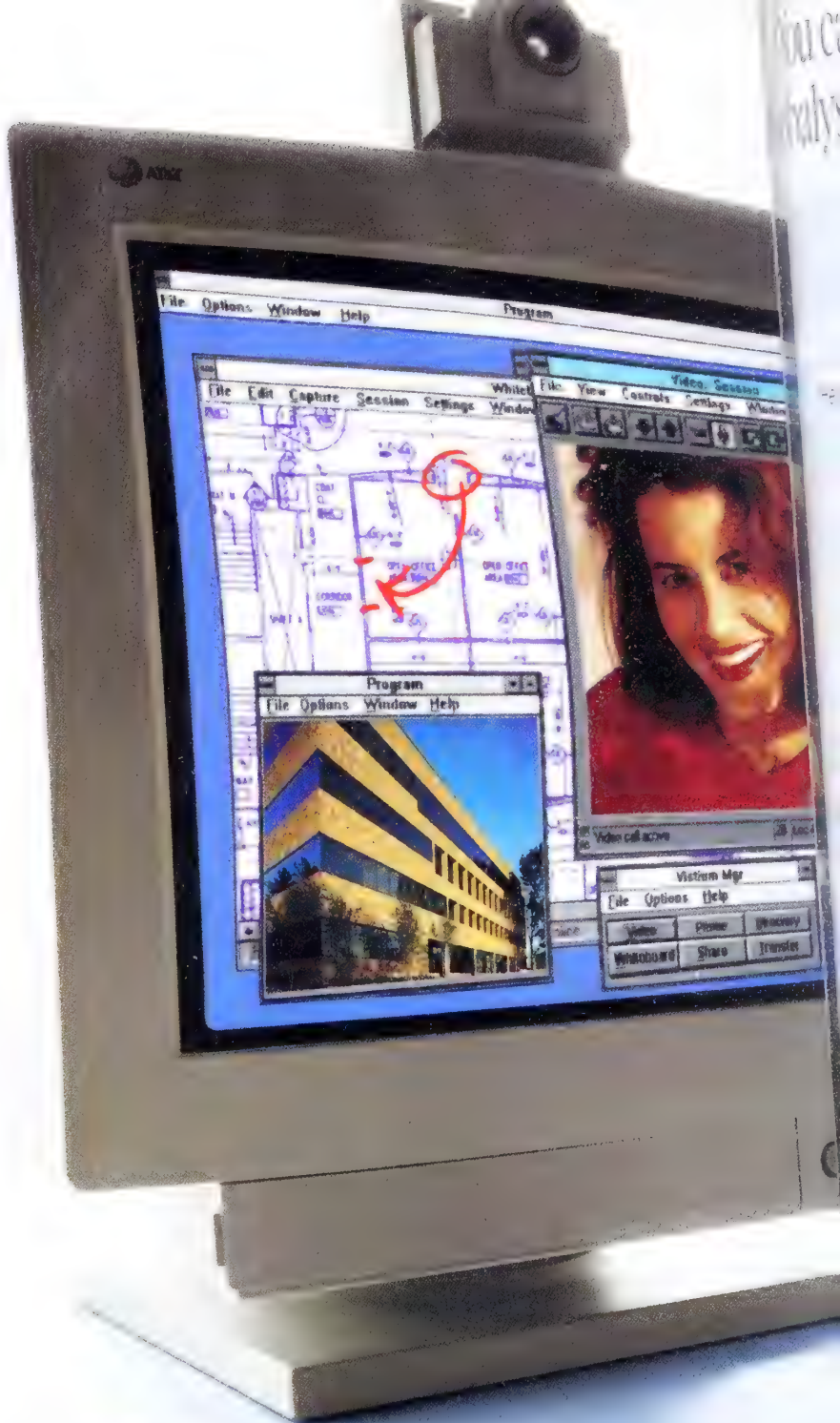
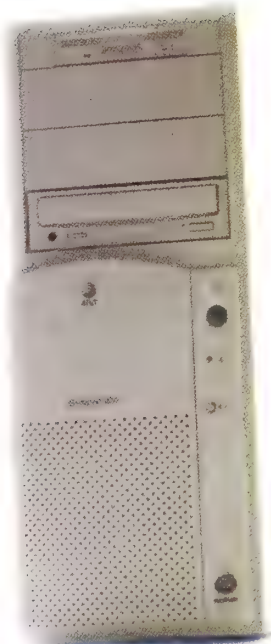
Many of the estimated 1 to 2 million women with silicone-gel implants are plotting their next move in the event no acceptable pact is reached. "It would be wonderful to save this deal," says Sybil Niden Goldrich, co-founder of Command Trust Network, a support group for implant recipients. "But to be further humiliated getting 5¢ on the dollar is absolutely out of the question." Two retaliatory measures under review: a boycott of manufacturers' products or a coordinated, massive opt-out by plaintiffs. Support-group leaders, who claim that ruptured silicone implants have disabled women worldwide, have begun circulating lists of products made by the various defendants in case a boycott is declared. "We know we can wield a lot of power," says Armstrong.

The industry may wield even more, given its financial muscle. As negotiation time grows short, the defendants are backing a campaign to sway public opinion and convince women that a deal is their best option. In the current probusiness climate in Congress, for example, breast-implant manufacturers have become the poster children of tort reform. Portraying themselves as victims of a legal system run amok, they have skillfully shifted the focus from the women's allegations to the plight of businesses unfairly accused of wrongdoing. Complaining about what they see as unreasonable demands by plaintiffs, one lawyer gripes: "We're talking about a larger amount of money than Clinton was able to garner from Japan and West Germany when he was trying to save Russia."

Dow Corning is now questioning whether to offer silicone in other products because of the liability it might face. To plead its case, Dow Corning ran full-page ads in 19 major newspapers nationwide in May. The message: No link exists between silicone gel breast implants and disease. "To pay large sums of money

of plaintiffs, and too little money add up to legal chaos





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for diseases we did not cause is unfair," says Dow Corning's Anderson.

The executive's beef comes after scientific research has shown no tie between silicone and a variety of maladies. Two recently published studies—one by the Mayo Clinic and another by Harvard University—found that women with silicone implants are no more likely to develop autoimmune or connective-tissue diseases than women without implants. The Mayo Clinic study compared the medical histories of 749 women who had implants with 1,498 who didn't and found no greater incidence of disease in one group than the other. Another larger, more comprehensive study is due out early next year.

**"DEAR DOCTOR."** The studies don't yet prove that the products are safe. And the Food & Drug Administration, which is still studying alarming rupture rates of the implants, will not allow gel implants to be used for anything other than reconstructive surgery anytime soon. It pulled them from the market in 1992. But these two studies and several others do weaken plaintiffs' claims that silicone-related diseases are widespread. "We now have a reasonable assurance that silicone-gel implants do not cause a large increase in traditional connective-tissue disease in women who have the implants," conclud-



ed FDA Commissioner David A. Kessler at an Aug. 1 congressional hearing. Added Dr. John S. Sergeant, a professor of medicine at Vanderbilt University School of Medicine: "The only thing keeping this issue alive is litigation."

To be sure that physicians are up on the latest science, a New York public-relations firm, The Dilenschneider Group, sent out on July 12 "Dear Doctor" letters to rheumatologists around the country. The goal of the campaign is to alert the specialists, who diagnose women making claims against implant manufacturers, to what Dilenschneider dubs the "junk science" plaintiffs' lawyers disseminate. Dilenschneider principal Matthew M. Swetonic, who declines to say for whom he's working, says he simply wants to get accurate information to doctors. Dow Chemical, Dow Corning, and Baxter all deny hiring Dilenschneider, while a Bristol-Myers spokesperson declines comment.

Plaintiffs' lawyers are considering launching their own PR machine to combat the industry's blitz. "We have to have somebody that can react to the total trash being put out there," says Houston attorney Richard N. Laminack, who represents 2,000 women.

Laminack's "total trash" refers to research that he and others contend is flawed and biased. The laundry list of deficiencies they allege includes the charge that researchers are focusing on the wrong diseases. Instead of probing traditional autoimmune sicknesses such as lupus and rheumatoid arthritis, these critics argue that an atypical disease made up of a hodgepodge of symptoms such as joint pain, fatigue, and hair loss should be studied. "The attorneys, FDA regulators, and scientists have

## VEXED IN ALABAMA

Federal judge S. Pointer sent the parties back to the drawing table: "certainly have but also serious doubts about whether it can worked out"

been looking for zebras when the surrounded by horses," says Dr. N. D. Anderson, an associate professor of medicine and surgery at Johns Hopkins University.

**SHORT TEMPER.** While the battles science rage, another war is on. Plaintiffs' negotiators are increasingly divided over the terms they'll accept in a new deal. "There's a civil war," says one lawyer. The rift, which has led lawyers to sort to name-calling and to storming out of meetings, pits class-action counsel against lawyers more versed in representing individual plaintiffs. The dispute has not only complicated the settlement talks but distanced the hundreds of lawyers nationwide representing implant recipients from their negotiating team. Plaintiffs' negotiators felt strongly that everything had to be done in secret," says Gary Troutwine, a lawyer representing 730 women. "As a result, they have come very, very isolated and are keeping other lawyers informed."

The plaintiffs' negotiators say the dispute is only natural in such a tense environment and that it is not impeding efforts to forge a new deal. "I've been walking out of meetings for two years. That's negotiation," says plaintiff lawyer Chesley, adding that bickering has to do with whether or not a new settlement can be reached by Aug. 30.

Instead, Chesley says it will come down to how badly all the parties want it. Everything else, he says, is posturing. "The defendants would like the public to think that these bad old plaintiffs' lawyers want to destroy Corporate America," he says. "If they like their case much, let them go to court." U.S. Judge Pointer grants the parties time, that could very well be wasted if everyone is headed.

By Linda Himmelstein in New York with John Carey in Washington and Keith Naughton in Detroit

## The Sticking Points

*For a global pact to work, negotiators must address the following issues:*

### WHO'S LIABLE AND FOR HOW MUCH

With scores more women than anticipated filing claims, more money is needed. But Dow Corning is in bankruptcy, and Dow Chemical refuses to participate in talks, so extra funds are proving tough to find.

### WHO WILL QUALIFY FOR COMPENSATION

Most women seeking compensation have ill-defined symptoms such as fatigue. Setting new criteria to qualify for money could knock plaintiffs with minor ailments out of the deal.

### THE STATE OF SCIENTIFIC EVIDENCE

Recently published studies cast doubt on whether silicone implants cause disease. Though inconclusive, the data have emboldened manufacturers to bargain harder.

**OPT-OUTS** A new deal will likely include an opt-out clause that allows plaintiffs to pursue cases outside the settlement. But too many opt-outs would hurt the pact, so negotiators are weighing whether to compel women into mediation.

A man in a brown suit and patterned tie stands next to a train car, smiling. The train car is dark with some text visible, including "ONE CAR" and "MAY 1987".

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# TOWERS OF STRENGTH

In many markets, commercial property is on the rebound

**I**t started as a few isolated cases. Then, slowly, almost imperceptibly, it spread across the country. Into apartments. Stores. Warehouses. Hotels. And now, offices. It may be in your very building.

What is it? The real estate recovery. After many fits and starts, the battered industry is finally on the rebound and picking up momentum. "The only thing holding the market back right now is the memory of the past five years, when people got badly burned," says Mark Zandi, chief economist at Regional Financial Associates Inc. (RFA) in West Chester, Pa.

The economic expansion gets a lot of the credit for helping shrink the industry's huge inventory of unused office space. Vacancy rates, though still high, are dropping in most office markets across the country. In some areas, rents are even rising, and hefty concession packages are no longer necessary to hook tenants. Indeed, in a few markets, ground is being broken for new office construction without even signing up tenants beforehand. And after years of being a drag or having little impact on the gross domestic product, commercial construction is picking up speed and actually adding to GDP growth. At \$164.4 billion, real spending on commercial structures is up more than 9% in 1995, compared with 2% growth in 1994 and drops in spending from 1991 to 1993, according to figures from RFA and the Bureau of Economic Analysis.

The most visible sign that the office sector is headed for better times is the battle for control over one of the world's

premier office properties, the Rockefeller Center complex in midtown Manhattan. Rockefeller Center Properties Inc., (RCPI), the real estate investment trust that holds the center's \$1.3 billion mortgage, saw the major owner of the property, Japan's Mitsubishi Estate Co., file for bankruptcy in May. Now, despite the loss of its interest stream from the mortgage, savvy investors are flocking to RCPI's doors. The draw: cutting a deal with RCPI that could eventually lead to an ownership stake in Rockefeller Center properties.

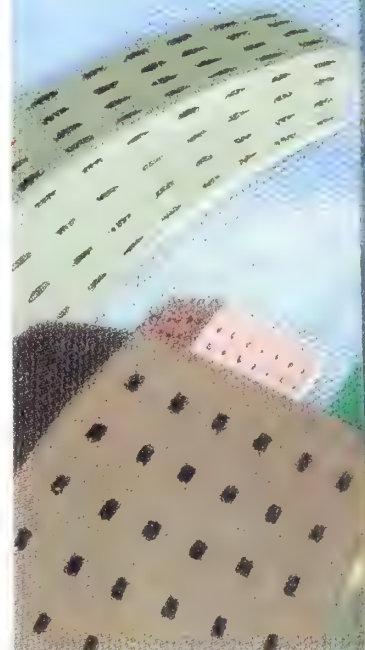
Two of the latest players trying to buy into RCPI are Chicago-based real estate magnate Sam Zell and New York developer Jerry Speyer. Zell says that top-flight office buildings are the best investment opportunity in real estate today. He expects such properties to improve steadily for the next 4 to 5 years and doesn't expect much new development for 3 to 4 years.



## PIECE OF THE ROCK?

Seeing a steadily improving market in top-flight office buildings, Chicago magnate Zell is trying to buy into Rockefeller Center

While midtown Manhattan is a hot spot, with vacancy rates from real estate firm Cushman & Wakefield showing a drop from 15.1% to 13.1% in the past year, the outlook for the downtown business district around Wall Street is gloomy. Granted, vacancy rates there dropped to 18.7% in 1995's first quarter, down from 19.4% in 1994's first quarter. But as companies relocate to the suburbs in search of more modern space and a better quality of life, the Wall Street area and other downtowns are suffering. That trend is reflected in the national vacancy rate for central business districts (CBDs), which, at 16.7%, is virtually unchanged from the prior year.



There are exceptions: Atlanta's vacancy rate slid from 22.6% to 16.6% in the first quarter, helped by pre-Olympics leasing activity. A growing financial services industry in Boston helped vacancies in downtown market drop from 13.1% in 1994's first quarter to 11.1% in the first quarter. But some areas, such as Dallas and Houston, which suffered massive overbuilding, still look dark. **COLD CASH.** The suburbs are another story. Even while downtown Dallas saw a sharp rise in its vacancy rate in the past year—from 33.5% to 37.1%, suburban Dallas' rate slid from 21.1% to 16.6%. Other suburban markets had steep declines include Seattle, which saw vacancies drop from 27.7% in 1994 to 18.8% in the first quarter of 1995, and Chicago, where the suburban rate fell from 18.6% to 15.4%.

Landlords in strong markets such as Charlotte, Raleigh-Durham, Atlanta and Las Vegas have even been hiking rents. And the increases are coming in cold, hard cash. In many other parts of the country, the gain comes in reduced need to entice tenants with month or more of free rent or improvements to space. Concessions such as free rent have virtually disappeared. Boston's suburban and downtown markets.

In some markets, demand is so strong that new construction is just around the corner. Peter Goodell, director of estate valuation and counseling at Evers & Lybrand, points to Phoenix,



compound annual rate of 2.4% from 1988 through 1994, according to the International Council of Shopping Centers. Use the same population figures to get the increase in real retail sales, however, and growth is just 1.5%, says S. Michael Giliberto, director of Lehman Brothers Inc.'s commercial property research team. Overbuilding in retail is actually worse than in office, says M. Leanne Lachman, of Schroder Real Estate Associates in Manhattan.

**NEW RULES?** The key to whether real estate experiences another boom-bust cycle lies in how much development capital flows back into the industry. Banks are likely to start lending again, but Zell thinks that there will be stricter standards for construction loans and that the days of virtually all-debt deals are over. Rents have been beaten down so much that borrowers would have

northern Virginia, and Washington, as areas where the income from is reaching a point where new development is close to becoming feasible. Development is already under way in Atlanta's Alpharetta suburb, where real estate company Cousins Properties Inc. is building a six-story office building of 126,700 rentable square feet "on spec"—before even lining up tenants. The first speculative office building to break ground in the Los Angeles area since 1990 is in the works in the Century City area, where the entertainment industry is riding high.

Construction is booming in the industrial sector of the real estate market, and warehouses. Here, the technology industry is fueling much of the growth. The sector is benefiting from

the need of high-tech manufacturers to expand into state-of-the-art facilities. Industrial vacancy rates have dropped to 7.4%, a 30% decline from a year ago, notes Michael Evans, national director, E&Y Kenneth Leventhal Real Estate Group. Zandi says that more than 50% of the increase in the sector over the past year comes from high-tech activities.

Another area where demand is starting to outstrip supply is in the apartment sector. Vacancy rates of 3% to 4% are not uncommon, and market rents are growing faster than inflation. The outlook is not nearly as bright for retail properties, such as shopping centers, however. When growth in retail shopping center space is divided by a population estimate, the result shows retail space per person growing at a

to show that rents on new projects would double by the completion of the project just to justify the deal, says Zell, adding that "even lenders aren't that stupid." Another check on the industry is the more stringent regulatory environment. "Today, we have risk-based capital rules, and enforcement is a lot stricter," says Leonard G. Sahling, Merrill Lynch & Co.'s real estate economist.

Will it really be different this time? After each boom-to-bust real estate cycle, bankers, investors, and developers have sworn that they've learned their lesson. But somehow, the promise of fat returns has a way of short-circuiting memories.

*By Suzanne Woolley, with Karen Pennar, in New York, and Richard A. Melcher in Chicago*

## RIGHTER AL ESTATE TURE

vacancy rates in seven  
town office markets

| DALLAS                                                                  |       |       | DENVER                                                                |       |      | LOS ANGELES                                                          |       |      | NEW YORK                                           |       |       |
|-------------------------------------------------------------------------|-------|-------|-----------------------------------------------------------------------|-------|------|----------------------------------------------------------------------|-------|------|----------------------------------------------------|-------|-------|
| 1                                                                       | 1994  | 1995  | 1991                                                                  | 1994  | 1995 | 1991                                                                 | 1994  | 1995 | 1991                                               | 1994  | 1995  |
| 6%                                                                      | 33.5% | 37.2% | 21.1%                                                                 | 16.4% | 15%  | 22.6%                                                                | 24.7% | 23%  | 17.2%                                              | 15.1% | 13.1% |
| Excessive overbuilding and quality of life issues plague downtown area. |       |       | Fast-improving region is benefiting from migration out of California. |       |      | Downtown LA remains in the dumps, but some submarkets are improving. |       |      | Big blocks of prime office space are hard to find. |       |       |
| DATA BY: CUSHMAN & WAKEFIELD INC.                                       |       |       |                                                                       |       |      |                                                                      |       |      |                                                    |       |       |

DATA: BW, CUSHMAN & WAKEFIELD INC.



## BANKS

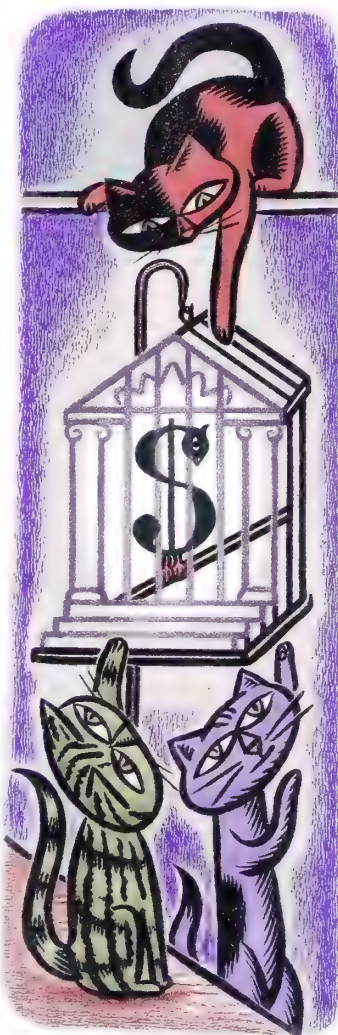
# BANK FRAUD, THE OLD-FASHIONED WAY

Bad checks are a far greater problem than high-tech heists

**W**hen a young Russian computer expert appeared in a London court on Aug. 17 accused of electronically robbing Citibank, bankers were seriously spooked. By allegedly penetrating Citibank's corporate cash-management system from St. Petersburg, siphoning off \$400,000, and trying to steal over \$10 million more, Vladimir Levin and his cronies raised the specter of online fraud being perpetrated against banks by outside hackers anywhere in the world.

Online fraud could eventually become an enormous problem, far outdistancing other forms of fraud. Indeed, as banks rush to offer new electronic banking services, crooks "are moving ahead faster than the security can keep up," warns Barbara E. Hurst, editor of *Bankers' Hotline*, a newsletter on security and compliance. But for now, the old-fashioned kind of fraud, especially involving checks, is a far more serious problem, costing banks billions every year. "While on occasion you will have a [breach] in an electronic system, I think you'll find the incidence of a break will be far less than the incidence of check fraud," says Dan McGurl, president of Bottomline Technologies, a Portsmouth (N.H.) maker of software designed to detect check fraud.

Check fraud dwarfs other forms of bank fraud (table). With Americans writing some 60 billion checks a year and technology such as desktop publishing making fraud ever easier to com-



mit, it is growing at an alarming pace. "The No. 1 loss for banks today is checks," says Robert H. Rasor, deputy assistant director of the U.S. Secret Service. "That whole system is kind of up for compromise." The American Bankers Assn. says incidents of check fraud rose 136% between 1991 and 1993.

The amounts of money involved in check frauds are rising as well. Rasor tells the story of a case dubbed Operation Paper Dragon, in which a single Vietnamese gang would descend on a town, print fake payroll checks purporting to be from the biggest local employer, cash them at various places in town, and then leave in a matter of days. That gang took in close to \$25 million and managed to operate for about seven months before being detected.

Technological advances are behind much of the rise in check fraud. Desktop publishing has made the manufacture

of fraudulent checks extremely simple. Frank W. Abagnale, a document security expert and consultant who is himself a onetime forger, says that for less than \$10,000, a would-be check counterfeiter can obtain the equipment necessary to produce fake checks in as little as 12 minutes.

**SCAN SCAM.** The procedure is simple, Abagnale says. First, to make the checks look legitimate, criminals scan in a company's logo as a background pattern for the paper. They can often obtain a company executive's signature from the annual report and scan that in

as well. Then, to obtain bank account information to put on the checks, call the company's accounts-receivable department, say they want to wire money, and request the necessary account number. "Today, there is no company in America that you can't call and say, 'I'm wiring you money. What are your wiring instructions?'" Abagnale says. Once the check is printed, it's a simple matter to cash it in a matter of minutes.

Banks are taking some steps to protect themselves and their customers. For example, many big banks now require corporate customers a system known as positive pay, which allows a customer to transmit to its bank records of checks issued each day. That way, a bank can reconcile the customer's list with checks presented for payment and identify any discrepancies. Don S. Tokunaga, director of security at First Interstate Bancorp, says a pilot program for fingerprint noncustomers trying to cash checks has dramatically reduced check fraud there.

For its part, Citibank says it is upgrading its internal security in the wake of Levin's alleged intrusion. A spokeswoman says the bank has added a security system that uses passwords

## Crime That Pays

*Financial fraud and its estimated annual cost*

|                                              |                                       |
|----------------------------------------------|---------------------------------------|
| <b>CHECK FRAUD</b><br>\$10<br>BILLION        | <b>ATM FRAUD</b><br>\$18*<br>MILLION  |
| <b>CREDIT-CARD FRAUD</b><br>\$712<br>MILLION | <b>ONLINE FRAUD</b><br>\$5<br>MILLION |

\* 1991 DATA AMERICAN BANKERS ASSN. BANKERS' HOTLINE

change every time they are used, no matter how fast the banks and regulators move to combat fraud, criminals are keeping pace. Regulators and banks are in an endless game of cat and mouse with criminals, even on the most sophisticated fraud, and experts say online fraud, while rare now, is still rising. "There is no bulletproof system," says Edward J. Hogan, senior vice president of MasterCard. And thanks to increasingly sophisticated technology, the bullets are getting more powerful every day.

*By Kelley Holland in New*



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# NOTHING SUB-PRIME ABOUT THESE PROFITS

Lenders embrace "impaired" borrowers—and make a bundle

**G**ary K. Judis, CEO of Los Angeles lender Aames Financial Corp., lives in a \$3 million home in Beverly Hills and in 1994 took home an annual salary and bonus of \$1.2 million. The approximately 6,000 customers who financed their homes through Judis' company have rather different balance sheets. Their credit ratings range from slightly flawed to plain awful [B, C, and D in lender's shorthand]. Most have missed at least one mortgage payment and are often also loaded down with car loans and credit-card debt.

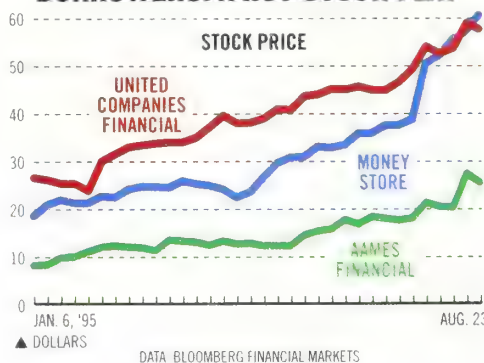
Judis' lofty lifestyle attests to the fact that catering to so-called sub-prime or impaired credit risks can produce super-prime profits. In the year ending June 30, Aames's revenue jumped 52%, to \$55 million. The company racked up a gross profit margin of 30%.

Lending to potential deadbeats was once regarded as barely a cut above loan sharking. Now many well-heeled finance companies are targeting this market. "The commercial banks have always sort of thumbed their nose and ignored the sub-prime borrower," says John Heffern, a NatWest Securities Corp. analyst. "That left a tremendous opportunity for smaller finance companies." Says Judis: "What we do has achieved a kind of legitimacy we just didn't have before." The stocks of some of the major players are sizzling. So far this year, Aames, the Money Store, and United Companies Financial are up on average an astonishing 236%.

**10% SOLUTION.** A variety of trends are driving the growth of the impaired credit business: the recent recession, corporate downsizing, and America's undying love affair with credit. But the alluring profitability derives from the



## LENDING TO TROUBLED BORROWERS: A HOT STOCK PLAY



ability of lenders to levy high fees and interest that more than compensate for the risks. In 1994, the annual interest rate on the typical Aames loan was 11.8%, several percentage points higher than the rate for "A" quality loans. Borrowers also have to shell out between 9% and 10% of the total loan value in up-front fees, compared to a recent average of 1.8% for an untainted bank borrower.

Fat profits are now luring traditional

mortgage lenders into the subprime business. Countrywide Credit tries, the nation's largest independent mortgage banker, began buying and C quality loans from mortgage originators in mid-August. Last September, Florida's Barnett Banks joined into the fray by acquiring EquiCorp., a sub-prime lender, for \$320 million in cash.

Sub-prime auto lenders have been targeted. In March, KeyCorp. it would pay \$305 million for the Finance Group Inc. and is now set to break into the highly fragmented \$65 billion-a-year, sub-par home lending market. More banks will predict A. Jay Meyerson, head of Corp consumer lending.

**"TIME TO WORRY."** Some observers, however, are concerned that these lenders could be in for trouble when the next recession hits. David Olson, a market researcher in Columbia, Md., worries that inflation, which in the past has bailed out many of the riskier loans, may not do the job next time around. "Whenever there's this kind of growth and euphoria, it's time to worry," Olson says. Adds Calvin Woelfel, director of Standard & Poor's Corporate set-backed unit: "We're

**AAMES CEO JUDIS: HIGH UP-FRONT FEES REDUCE RISK**

companies like increasing their acquisition rates, and ge-

ly taking on more risk."

Already there is evidence of trouble. In March, Search Capital Group, a prime auto lender in Dallas that went public in December, 1993, was delisted by NASDAQ after losing \$26 million in 1994. According to Robert Idzi, the company's new chief financial officer, Search Capital erred by using \$90 million in 1993 debt and equity offerings to make "a riskier category of loans as much as 125% of a car's value."

Judis believes Aames has its business under control. For one thing, he says, the company lends only 55% of a borrower's value to risky borrowers. And although Aames's foreclosure rate rose sharply for four years, it plunged in the nine months of the 1995 fiscal year ended June 30 to under 2%, a drop of more than half from 1994 levels.

Nor is Judis concerned about the prospect of new competitors or about federal disclosure rules that take effect in October. Some experts fear the rules could raise costs for subprime lenders. Responds Judis: "As long as you have a credit system, you'll have people who abuse it." Lucky for him.

By Nanette Byrnes in Los Angeles



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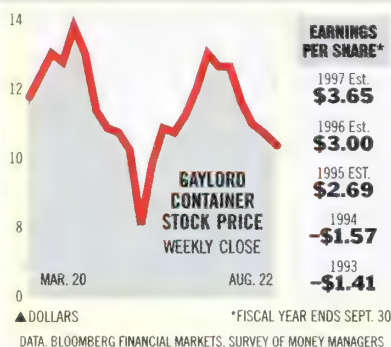
BY GENE G. MARCIAL

## BUYERS SIZE UP A TIDY PACKAGE

**C**all it the Comeback Kid: After four years of red ink, Gaylord Container (GCR) will be in the black this year. Analysts have been raising their 1995 and 1996 earnings estimates, but Gaylord, a producer of linerboard and containerboard, may exceed even those revisions, say several big stakeholders.

That's not the only reason investors have been accumulating stock. They say a major paper and forest-products company has been doing homework "in

### GAYLORD'S ROUGH PATCH



preparation for making a buyout offer for Gaylord," whose shares trade at 10. These pros put Gaylord's takeover value at 20, based on a business pickup—fueled by firming prices and increased demand.

"Gaylord is a pure play in linerboard and containerboard," says one big investor. He notes that several paper companies have been filling billion-dollar war chests for acquisitions. At 20 a share, Gaylord's price tag would be \$1.2 billion. "Almost all the industry biggies want to be larger players in linerboard and containerboard, too," this pro says.

One big stakeholder notes that Gaylord, despite recent dire straits, is rebounding smartly, with strong earnings growth (chart). On the other hand, Gaylord's stock is selling at "very cheap price-earnings and price-to-cash-flow ratios," he adds. The stock is trading at 3.7 times the 1995 profit estimate, vs. an average p-e of 8.4 for its peer group, and 3 times the 1996 projected earnings, vs. 6.2 for the group.

This pro figures Gaylord will earn \$2.69 a share this year, \$3 in 1996, and \$3.65 in 1997—way above analysts' es-

timates. According to Zacks Investment Research, the mean estimates are \$2.29 for 1995 and \$2.69 for 1996.

Linda Lieberman, an analyst at Bear Stearns, rates the stock an "attractive" buy on fundamentals alone. Her target for the stock price on that basis is 15 to 17 a share. Of note, she says, is the way the company has been paying off debt: In the past two months, Gaylord has paid down \$40 million of its bank term loan, and a total of \$73 million since January. Gaylord, she notes, has long-term debt of \$645 million. Gaylord says it doesn't comment on rumors.

## IS THE SUN RISING ON WORLDCORP?

**T**he name WorldCorp (WOA) makes this company sound as if its two operations would be naturals as global winners. That's what some money managers are betting on. Its US Order unit, which provides transaction-processing software for home-banking and network-telephone services, has deals with Visa International and Britain's Barclays Bank. And its World Airways has piled up a contract backlog of \$463 million, a big jump from last year's \$36 million.

WorldCorp, mentioned favorably in this column back in February, when it was trading at 8½, is now at 12. And Will Weinstein, senior partner at Genesis Merchant Group Securities in San Francisco, says its underlying assets are worth 20. Weinstein notes that WorldCorp is trading at 10 times estimated 1996 earnings of \$1.21 a share. For 1995, he expects the company to make only 10¢ a share. But a quantum leap is coming: US Order, which has yet to make money, will start producing "bountiful profits next year," says Gary Craft of Genesis. WorldCorp will take World Airways public in early October and reduce its stake in it to 59%. The carrier also expects big profits next year, says Craft.

World Airways is an international operator of charter flights for passengers and cargo for government and commercial customers. Its business includes jet leasing and providing other services for the U.S. government, Malaysia Airlines, and Garuda Indonesia.

WorldCorp took US Order (USOR) public in June at 13½ a share—retaining a 61% ownership. Visa has paid \$15 million for about 60% of US Order's operating assets. US Order will get royalty payments from Visa on cus-

tomers that use its technology. 60 banks have agreed to use its interactive system.

## SWAMPED BY INCOMING CALLS

**B**ells are ringing at WorldCom (formerly LDDS Communication), nation's fourth-largest long-distance carrier, which is apparently buyout-bait. Takeover speculation started when billionaire John Kluge, WorldCom's man and largest stakeholder, announced on Aug. 14 he was selling his stake. And Kluge's 30.8 million shares got snapped up quickly. The stake held by Kluge through his Metron Co., went for 30%. The stock closed at the same price on Aug. 22.

"The many deep-pocketed players eager to buy into fast-growing WorldCom, suggest buyout interest is strong," says one New York investment banker. Some pros whisper one big buyer is Electronic Data Systems, which is being spun off by General Motors. "Expect EDS to announce it has acquired more than a 5% stake in WorldCom," he says. EDS may take over its stake for a while until ready to make an offer, he adds.

One big investor figures that WorldCom would be worth \$47 to \$50 a share in a takeover. "CEO Bernie Ebbers has done a tremendous job of sharply increasing the company's sales and earnings," he adds. EDS, a leading computer-service outfit, would be able to provide its customers combined computer and phone services if it had WorldCom's assets and operations, he explains. Other rumored potential suitors include Sprint, GTE, and the Baby Bells. "But cash-rich EDS has the best chances of convincing Ebbers about a deal," says pro. Ebbers says "to my knowledge none of the [rumored suitors] has bought shares." Like any public company, he adds, any offer would be subject to holders' approval. "But no approval has ever been made."

### WORLDCOM HAS A BEVY OF SUITORS





## COMMUNICATIONS

# UNPROVEN, BUT DAZZLING

Qualcomm is on a roll with its cell-phone technology

Seven years ago, Qualcomm Inc. was a tiny but not unimpressive thorn on the outside of the cellular industry. The ego satellite communications company came up with a scheme for expanding cellular capacity, vitally important in regions where frequencies are saturated. The problem: The industry had already set a method for just that. Qualcomm muddled the waters with an alternative as theoretically superior and offered better quality, but no one knew whether its patented technique would work.

They still aren't sure—but Qualcomm is on a roll anyway. It has signed up 10 of the 14 largest cellular operators to use its proprietary digital technology, CDMA, for code-division multiple access, even though it has yet to be used in a commercial setting. And this year, in stunning back-to-back decisions, two of the biggest in the Federal Communications Commission's auction of licenses for mobile communications services (PCS) reportedly said that they, too, would



be using Qualcomm's technology. The 10-year-old company's stock rose along with its fortunes, from 26 in February to a record high 54½ on Aug. 16, before dropping back to about 48, where analysts say it is fairly valued. It also rushed out a public offering on Aug. 9, raising nearly a half-billion dollars.

Qualcomm wants the money so that it can stop licensing its technology and start manufacturing gear itself. President Harvey P. White figures the industry's move to CDMA gives Qualcomm a once-in-a-lifetime chance to make the

leap to the major leagues of the telecom equipment business. "I think wireless [equipment] could become a \$40 billion-a-year business," predicts Qualcomm founder and CEO Irwin M. Jacobs, "so there's plenty of room for more manufacturers." Montgomery Securities analyst Matthew S. Robinson says Qualcomm's move into cellular equipment could push its revenues to \$1 billion by 1998, from \$385 million for the year ending Sept. 30 (chart).

Manufacturing isn't a new game for Qualcomm. As the world's largest satellite-based mobile communications company, providing communications and position information to truck fleets, it makes the equipment that goes into each truck as well as selling the service. Beyond telecom, Qualcomm is known for Eudora, the most widely used Internet electronic mail package. "Lots of students use it, and every time they use it, 'Qualcomm' pops up on the screen," boasts Jacobs.

### PREACHING

**Qualcomm CEO Jacobs is spreading the digital gospel with a lower-cost, more-powerful standard**

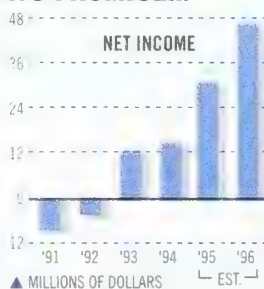
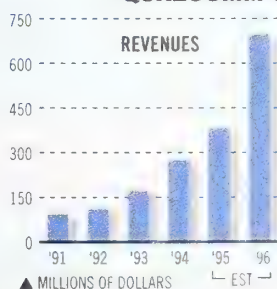
CDMA, though, is Qualcomm's ticket to the big time. The company has a 51% stake in a \$61 million manufacturing venture with Sony Corp. that is revving up a San Diego factory to churn out up to 1 million phones a month by yearend. Qualcomm is also

getting ready to manufacture the base stations that are used in wireless networks, which Northern Telecom Ltd. has agreed to bundle with its cellular and PCS switching systems for the North American market. "If Qualcomm can bring in enough industry expertise, or if it can develop successful joint ventures, then it can be a significant manufacturing force," says John B. Ledahl, analyst at market researcher Dataquest Inc.

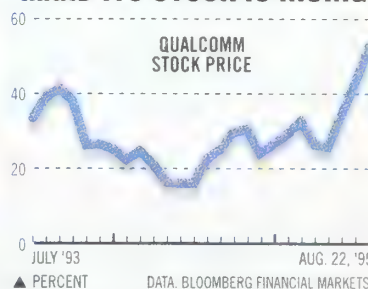
Still, Qualcomm is only a tenth the size of its next-larger equipment com-

Breaking  
out of the  
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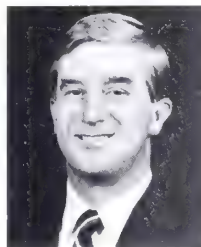
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petitor. It has no way to match innovative financing plans that companies routinely offer systemtors. Instead, Qualcomm is taking its positions in overseas cellular nies, such as Korea's Shinsegi T Inc. and Chile's Entel Telefonía M that it can have some clout as technology they choose.

**OLD PROBLEM.** And it keeps w CDMA converts at home. Some ke ers are still resisting—AT&T's M Cellular, the largest U.S. cellula ator, is rolling out a competing t ogy called TDMA, for time-division ple access. But CDMA's lower co convinced the Bell Atlantic-Nynex less joint venture. "We had TDM few markets, largely for comp reasons. We did not actively p it," says a spokeswoman for the The group is switching to CDMA a long haul.

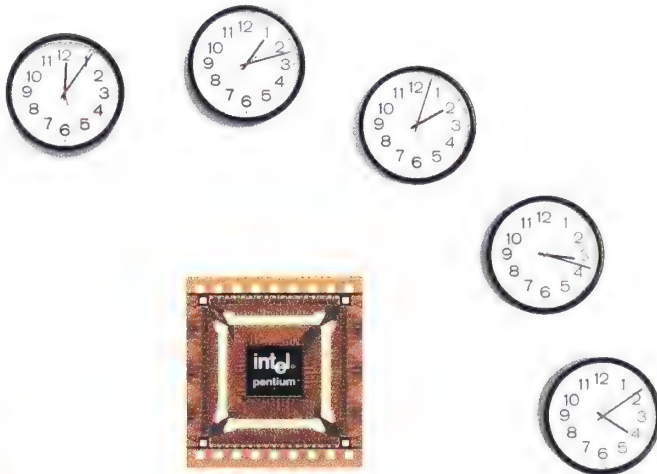
Both technologies address the problem—lack of capacity. Today's lar systems devote a single chan each conversation. TDMA, adopted cellular industry as a standard it can increase capacity threefold by each conversation into tiny piec running them sequentially. C means to create 10 times more c by chopping up the calls and spr them across all available chan needs only one-half to one-third tennas to achieve the same covere TDMA, because it can maintain quality over a longer distance.

The lower cost looks to make hit in the emerging PCS industr biggest PCS bidder, Sprint Teleco munications Venture, a joint ventu tween Sprint Corp. and four ce partners, has announced it will CDMA in 29 markets. PrimeCo, a nership between U.S. West Atlantic, Nynex, and AirTouch, w go with Qualcomm technology because of its lower cost. "CD quires fewer cell sites, and th pivotal in the PCS decision," s Craig Farrill, vice-president fo nology planning and developm AirTouch Communications Inc.

A lot is riding on AirTouch. launch the first commercial CDMA this fall, an upgraded cellular netw Los Angeles. The launch has a been delayed a few times by pr with sound quality and interf from analog signals. Still, says AirTouch's trials show capacity ing by 8 to 12 times. That's the test result that Qualcomm devote to hear about.

*By Larry Armstrong in San*

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# PUTTING HUNGARIAN HIGH TECH ON THE MAP

From disks to software, hundreds of startups are thriving

... Kürti learned that disk drives the real way. As an electrician in Hungary in the 1970s, he repaired the transistor-era computers by a state-run electronics company. A Western technology sales last bloc meant few parts, fewer manuals, hours of tinkering.

... all that patience is off. Kürti boasts 2,000 customers for his tech business, Kurtech, which recovers data from crashed hard disks. When the company got its slow start in 1989, it was expected to double in a year, to \$8 million. Customers ranging from banks to the German government pay an average of \$10,000 to rescue their data. "We say we'll have as many as Kürti's brother-in-law, Sándor, who is an engineer."

**ENTREPRENEURS.** That mix of power and drive is something new in Hungary: small but viable tech companies. In the past few years, more than 100 startups have sprung up, ranging from biotechnology to their own

But a growing number of highfliers are going head-to-head with niche rivals in the U.S. and Japan. Says Esther Dyson, who runs a New York-based venture capital fund specializing in East European technology companies: "There is a shortage of ideas. The potential for tech startups is huge."

Hungary isn't the only home to high tech in the region, it stands out because it had a headstart. Elite Hungarian universities have long produced excellent scientists, including several



## Venture capital is pouring in, which is critical since banks charge 36% interest on commercial loans

Nobel prizewinners. In the 1980s, Hungary's attempts at economic reform allowed researchers to leave their labs and set up their own small businesses. Although many scientists left the country for better wages and labs after 1989, those who stayed behind have since gained free-market experience. They're beginning to make their mark.

Take Graphisoft. Back in 1982, Gábor Bojar, an enterprising mathematician, left the Hungarian Geophysical In-

stitute and teamed up with a friend to design programs for three-dimensional screen displays. During years of working on programmable calculators and awkward Russian computers that kept breaking down, the pair learned to write extremely compact computer instructions. In 1983, executives from Apple Computer Inc. discovered Bojar at a Munich trade fair. They encouraged him to develop a program designed for architects using the Macintosh. Now, Graphisoft designs and markets ArchiCAD software used by architects around the world. Last year, sales totaled \$12.5 million, mostly overseas. The company has units in the U.S., Germany, and Japan.

**FLEXIBLE FIND.** Then there's Gábor Prózský. A mathematician and linguist, he set up a software maker called Morphologic in 1992 with friends from Technical University of Budapest. Morphologic won a contract with Microsoft to provide the spell-checker, hyphenation, and thesaurus programs on the Hungarian version of Microsoft Word, having provided similar programs for Lotus and WordPerfect. The underlying software was so flexible that Microsoft is talking with Prózský about handling the versions in Polish and Romanian.

As the high-tech sector takes off, more venture-capital companies are piling into Hungary. That's critical, because banks charge 36% interest on commercial loans, making borrowing next to impossible for many entrepreneurs. The \$120 million First Hungary

Fund, for example, provided a crucial \$16 million investment in Biorex, a pharmaceutical company created by Péter Literáti, a leading research scientist. The money helped him to develop a compound to prevent the side effects of diabetes. It's undergoing trials in Britain. Says Peter Rona, chairman of the fund: "It was a long shot."

To be sure, Hungary's high-tech sector still faces its share of problems. Scientists often lack management and marketing expertise, and it can be an uphill battle convincing customers that Hungarian companies can outdo Japanese or American rivals. Even so, the Hungarian scientists that stayed behind are making an increasingly significant contribution to their economy. Not only are they providing jobs, they're also showing other fledgling entrepreneurs that Hungary can indeed find a niche in the world market for high tech.

*By T.R. Smart in Budapest and Karen Lowry Miller in Bonn*



EDITED BY AMY DUNKIN

# WANT TO HEDGE YOUR BET ON THE BULL? TRY OPTIONS

**S**tock jocks should be feeling pretty pleased: The Dow Jones industrial average is up 20% for the year, and equity portfolios are showing handsome returns. But success can breed anxiety. In the past few weeks, the market has hovered in the 4600 range and has suffered some scary one-day declines. If it tanks, your hard-won gains could fade. Yet if you take the profits, you'll owe a hefty chunk in capital-gains taxes, and worse, you could miss out if the bull continues to run.

Experienced investors can resolve this dilemma using stock options. But before you venture into this realm, make sure you've considered more basic ways to reduce risk. Diversification is one of the most fundamental ways to hedge, since the more sectors you're invested in, the more likely it is that some will go up when others go down. During high-flying times such as these, you could put more emphasis on stocks that tend to do well when the market declines, such as gold and energy. You might buy into mutual funds, such as Dreyfus'

Comstock Partners Strategy fund and Rydex Ursa portfolio, that are designed to shine in down markets. Or you may simply want to move more of your assets into cash.

If such measures seem old hat and you've crafted a finely tuned portfolio you don't want to disturb, you ought to consider options, which are simply contracts allowing you

to buy or sell 100 shares of stock at a fixed price by a specified date. In contrast with more basic strategies, options offer a precise way to protect a single stock, a specific sector, even a whole diversified portfolio.

Stock options are leveraged, so you need only put up a small amount of capital to produce gains substantial enough to make up for dra-

matic losses. But unlike leveraged bets you can by selling stocks short, playing index futures, options losses can be to the premium you paid, the prospect of unlimited losses, should picked up, makes futures and selling too risky for many investors, says Scott Fuchs, chief options strategist at Swiss American Securities.

Writing a covered call is an entry-level options strategy. Essentially, you sell a call option to an investor the option to buy your stock at a set price within a certain time period. You pocket the cash premium. (Of course, the changes act as intermediaries between buyers and



## INVESTING

You can buy put options as "crash protection," the way you buy collision coverage on your car



you have to pay commissions.) That set known as the striking usually, you would pick itly above the stock's trading price. The er of the call hopes k price will climb, at int that person could the right to buy the ore cheaply. So if ck rises above the price, it probably alled away, and you'll sell it, unless you again to buy back on. But if the stock at or declines, you premium, along with ding.

s how it might work: 1 100 shares of Mot- trading at 76%. After a 46% total return ast year, you decide k has nowhere to go vn. So you write a call with a strike 80, allowing whoever s the call to pay you are for your stock. ket the \$275 premi- he option sale. If the mbs above 80, your ill be called and you l, missing out on gains. If the stock hange or drops, you ur shares and the 1.

**SHOT.** Covered calls isidered a hedging because the premi- rides a cushion that e up for losses when ck declines in value. stocks make the best es, since you get a remium for them. But a call option is not go- ash-proof your portfo- ions Bernard Shaeffer, t of the Options In- which publishes news- n options strategies.

really want to cover losses, you need to put options. Puts, the of calls, are the right stock at a set price stated time frame. To our Motorola holding, d buy an option to sell es of Motorola at 75 mid-October, paying remium for that right.

Then, even if the stock falls through the floor, you have locked in a selling price of 75. If the stock rises in price, your option expires and you'll be out the \$300. You can trade options before they expire, but if you are hedging, you should leave them in place as long as possible.

Don't mourn an option that

but you can hedge for up to three years using long-term equity anticipation securities, or LEAPS.

You can also save money on put options by picking a low strike price—meaning you'll tolerate a large decline in value before selling the stock. The purest hedge is “at the money”—when the

## How One Hedge Might Work

*Since put options increase in value when stock prices fall, you could protect a diversified stock portfolio from a sudden market decline by purchasing puts in the Standard & Poor's 100 Index, known as “OEX.”*

**1** You determine you'll need five put contracts to protect your \$250,000 portfolio by using this formula: Divide the stocks' value by the value of the index\* times the underlying number of shares, which is most often 100. The math in this case: \$250,000 divided by (529.59 X 100).

**2** You only want the protection for the next two months, so you purchase contracts that expire in the middle of October. You buy “at the money” puts at a strike price of 530. They trade at 9½ points, or \$950 per contract, so you need to shell out \$4,750 for this “insurance.”

**3** Should the market suffer a 10% correction, your portfolio would decline by \$25,000. The puts, at expiration, would be worth 53.67 points per contract, resulting in a gain of \$22,085, or about 88% of your portfolio's losses. If the stock market fell 20%, the puts would recapture 96% of your losses.

**4** If the stock market continues its ascent or remains flat, the options expire worthless, and you are out the \$4,750 you paid for them.

\* All prices are as of Aug. 15, 1995

DATA: SWISS AMERICAN SECURITIES INC.

expires worthless. Instead, think of it as an insurance policy. Just as you buy collision coverage on a car while hoping you won't have an accident, you should buy put options as “crash protection,” hoping you won't need them, says Richard Mikaliunas, who is in charge of marketing derivative securities at the American Stock Exchange.

Also, as with other insurance policies, you can negotiate a lower deductible if you're willing to assume more risk. For example, the longer the time period until the option expires (from one to seven months for standard options), the more expensive it is. A one- or two-month time frame is the most economical,

market value of the stock is the same as the striking price on the option. You can save on premium costs with an “out of the money” contract, where the stock value is higher than the striking price. The more “out of the money” you go, the less expensive the contract. For example, the same Motorola put with a striking price of 70 would cost \$137.50.

If you're worried about a group of stocks, it may be easier to protect them all at once rather than individually. You can buy an option on a broad-based index or on an index that tracks a specific sector. If you're worried that your semiconductor stocks might crash, says Swiss

American's Fullman, buy a put on the Philadelphia Semiconductor Index. Or if you're shielding a diversified portfolio of large-capitalization stocks, try the Standard & Poor's 100, a very liquid index that often matches holdings of individual investors.

Buying a put option on an index is similar to buying one on a stock, except index options are settled in cash. The put's value rises as the index value drops. If you do nothing and the index value declines, the exchanges exercise the option just before expiration and deposit the cash in your account.

**STAY COOL.** The biggest danger of hedging with stock options is that you'll grow so enamored of the potential for huge short-term gains that you'll start speculating, says Michael Braude, president of the Kansas City Board of Trade, which markets options on its Mini Value Line Futures contract as a hedging tool for individuals. The reason so many people grow to detest options and futures is not because they hedged but because they gambled and lost, he says.

Another danger is that you'll start trying to time the market. Once you buy a put, you'll have to watch options prices daily and learn to make quick buy and sell decisions. “They cause you to do the things a short-term trader does,” says Shaeffer. Besides, he says, options can get costly: “You can get yourself into a psychology of having to keep buying new puts as old puts expire.”

But even conservative financial planners say this may be a good time for smart investors to make a first foray into options. “Let's face it,” says Daniel Masiello, a Staten Island (N. Y.) planner with American Express Financial Advisors Inc., “this bull market can't go on forever.” And if the prospect of watching your gains erode is making you queasy, stock options could be just the tonic you need.

Amey Stone







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## SHOW-AND-TELL TUTORS FOR WINDOWS 95

*"Dear Auntie Virus: No matter what I do, I can't bring my computer into the '90s. Every time I try to get onto the Information Superhighway, my DOS gives me Das Boot....I love my little 286, but using it makes me*

watch demonstrations, they provide advantages over text-only training.

Graphix Zone is hoping humor is the way to get non-propeller heads to absorb an often-dry topic. Next to real meanings in a glossary are silly explanations. "Device" is defined as "de guys who busted Joey Buttafuoco."



*feel like I'm stuck in 1986...and I hated that gear. Signed, Stuck in the '80s."*

*"Dear Stuck: What you need is to get...a machine that runs Windows 95...."*

If that seems like a funny way to get into Windows 95, that's kind of the point. Auntie Virus is a character in *The Improv Presents Windows 95 for the Technically Challenged*, from Graphix Zone, an interactive CD-ROM aimed at helping people conquer the Win95 learning curve.

With the arrival of Microsoft's new operating system comes a slew of multimedia CD-ROMs and instructional videos for people who don't want to slog through a manual written in computerese or one of the hundreds of commercial books available. And by letting you try out Win95 yourself or

Throughout the program, an emcee introduces the video characters who run Win95 classes, played by comics who have worked the Improv nightclub stages nationwide. Ditzzy flight attendant Nan O'Second pilots a lesson called "Using Windows Help... As a Flotation Device." Sergeant Systems USPC takes users through software basic training. And Julia Files helps people "Get Cooking With Applications...."

**YUKMEISTERS.** Although the Improv disk contains some funny bits, the laughs didn't sustain my interest. Fortunately, not all training CD-ROMs rely so heavily on attempted humor. One that I can recommend with a few reservations is *Easy Tutor Learn Windows 95* from CRT Multimedia.

With *Easy Tutor*, users can choose how deeply they

want to explore Win95. There are 10 "how to" modules that include exercises on customizing the desktop and running programs. People can try Win95 tasks themselves, watch the computer demonstrate how things are done, or see (whenever applicable) how Windows 3.1 handled the same task. A "concepts" area uses animated cartoons to explain the benefits of some new Windows 95 features, and there's a quiz to test your knowledge. But some of its tips

quires Win95 and is supposed to work seamlessly with new operating systems. The five-chapter course provides demonstrations and step examples of features. Classes can be customized for Windows newcomers and upgraders.

Two former Microsoft Windows product managers are the trainers in a new called *Learn! Microsoft Windows 95 Getting Started*. WinStruct (800 242-4841) is first in a three-tape (\$20 each or \$55 for the

### SOFTWARE

## Learning an Operating System

PRODUCT/PRICE/PUBLISHER

**EASY TUTOR**  
**LEARN WINDOWS 95**  
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**LEARN! WINDOWS 95**  
**GETTING STARTED**  
\$20 each. WinStruct

COMMENTS

Straightforward CD-ROM gives users hands-on lessons. Includes quiz and glossary of Win95 terms.

Nightclub comics play characters who steer an audience through Win95. The CD-ROM has funny spots but soon grows tiresome.

Videotape is first of three. Former Microsoft Windows product managers help viewers with differences between Win95 and older versions.

DATA BUSINESS WEEK

are lame. ("The start button is great. Try using it when you start your session.")

Both *Easy Tutor* and the *Improv* disk work on computers running Windows 3.1 or Windows 95. The \$50 CD-ROM *Microsoft Windows 95 Starts Here*, available in September from Microsoft Press, re-

a cybersitcom that uses about half of the one video (soon to be a CD). The sitcom is filled with jokes ("Plug and What's that, some keyboard hair replacement for keyboards?"). With lines such as "This might as well just read the manual." Edward

### WORTH NOTING

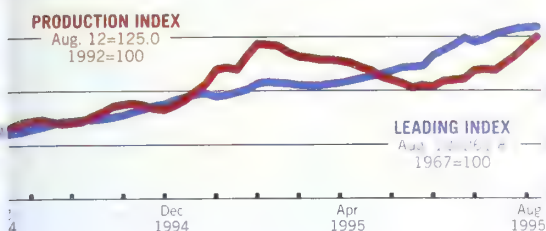
■ **HALLOWED HALLS.** While you probably know baseball's museum in Cooperstown, N. Y., you may not be familiar with the other halls of fame in North America. New book, *The Volvo Guide to Halls of Fame* (Living Planet Press, \$12.95, 800 345-6665), profiles more than 1,000 such places, honoring everything from Barbie dolls to questionable medical devices.

■ **UNCLE SAM SALES.** To find out how to buy government property—from computers to jewelry to tractors—order the *Guide to Federal Government Sales* (Item 143B, \$1.75) from Consumer Information Center, Pueblo, Colo. 81009. For info about real estate sales you can also send for the *U.S. Real Property Sales* (Item 515B, free). It's updated bimonthly.

# Business Week Index

## PRODUCTION AND LEADING INDEXES

Change from last week: 0.7%  
Change from last year: 4.8%  
Change from last week: 0.0%  
Change from last year: 8.3%



The production index increased during the week ended Aug. 12. But before the four-week moving average, the index fell sharply, to 123.8 from 125.1, as seasonally adjusted output levels of autos, trucks, paper, and power dropped.

The leading index was little changed in the latest week, and the unadjusted index rose to 262.3, from 261.5 in the previous week. Higher stock prices and growth rates for materials prices and M2 led the increase.

Production index copyright © 1995 by The McGraw-Hill Companies. BW leading index copyright 1995 by CIBC

## FINANCIAL INDICATORS

|                                          | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|------------------------------------------|-------------|------------|--------------|
| <b>PRICES</b> (8/18) S&P 500             | 559.31      | 558.54     | 20.6         |
| <b>FIXED RATE BOND YIELD, Aaa</b> (8/18) | 7.64%       | 7.58%      | -5.3         |
| <b>COMMODITY MATERIALS PRICES</b> (8/18) | 113.8       | 114.0      | NA           |
| <b>STOCK MARKET FAILURES</b> (8/11)      | NA          | NA         | NA           |
| <b>STATE BONDS</b> (8/9) billions        | \$493.2     | \$491.6r   | 12.0         |
| <b>SUPPLY, M2</b> (8/7) billions         | \$3,695.7   | \$3,687.0r | 3.3          |
| <b>CLAIMS, UNEMPLOYMENT</b> (8/5) thous  | 332         | 321        | 2.2          |

Source: Center for International Business Cycle Research (CIBC), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of companies), Federal Reserve, Labor Dept. CIBC seasonally adjusts data on failures and real estate loans. \*Historical data available from CIBC

## BEST RATES

|                                            | LATEST WEEK | WEEK AGO | YEAR AGO |
|--------------------------------------------|-------------|----------|----------|
| <b>MUTUAL FUNDS</b> (8/22)                 | 5.68%       | 5.90%    | 4.66%    |
| <b>COMMERCIAL PAPER</b> (8/22) 3-month     | 5.83        | 5.86     | 4.90     |
| <b>RATES OF DEPOSIT</b> (8/23) 3-month     | 5.78        | 5.80     | 4.87     |
| <b>MORTGAGE</b> (8/18) 30-year             | 8.20        | 8.02     | 8.69     |
| <b>ADJUSTABLE MORTGAGE</b> (8/18) one-year | 6.05        | 5.91     | 5.66     |
| (8/23)                                     | 8.75        | 8.75     | 7.75     |

Federal Reserve, HSH Associates, Reuters Holdings PLC

1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### HOME SALES

Aug. 29, 10 a.m. ▶ New houses sold at an annual rate of 700,000, says the median forecast of economist surveyed by MMS International, one of the major firms. Sales in June rose at a 728,000 pace.

### CONSUMER CONFIDENCE

Aug. 29, 10 a.m. ▶ The Conference Board's confidence index likely rose to 99.9 in August, up from July's 99.9.

### DOMESTIC PRODUCT

Aug. 30, 8:30 a.m. ▶ According to the MMS survey, the Commerce Dept. second look at the second-quarter

gross domestic product data will probably show no revision to the 0.5% annual rate of growth originally reported. The economy grew at a 2.7% pace in the first quarter.

### PERSONAL INCOME

Thursday, Aug. 31, 8:30 a.m. ▶ Personal income likely increased 0.5% in July, on top of a 0.4% gain in June. That's suggested by the jump in nonfarm weekly pay. Consumer spending probably edged up 0.3% in July. June outlays rose 0.2%.

### LEADING INDICATORS

Friday, Sept. 1, 8:30 a.m. ▶ The composite index of leading indicators likely rose 0.1% in July, after a 0.2% gain in June.

## PRODUCTION INDICATORS

|                                                        | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|--------------------------------------------------------|-------------|-----------|--------------|
| <b>STEEL</b> (8/19) thous. of net tons                 | 1,873       | 1,922#    | 3            |
| <b>AUTOS</b> (8/19) units                              | 95,717      | 103,549r# | -24.5        |
| <b>TRUCKS</b> (8/19) units                             | 112,079     | 107,665r# | -8.4         |
| <b>ELECTRIC POWER</b> (8/19) millions of kilowatt-hrs. | 79,332      | 74,474#   | 16.7         |
| <b>CRUDE-OIL REFINING</b> (8/19) thous. of bbl./day    | 14,157      | 14,236#   | -1.4         |
| <b>COAL</b> (8/12) thous. of net tons                  | 19,853#     | 18,505    | -2.6         |
| <b>PAPERBOARD</b> (8/12) thous. of tons                | 902.4#      | 906.8r    | 2.9          |
| <b>PAPER</b> (8/12) thous. of tons                     | 847.0#      | 852.0r    | 0.4          |
| <b>LUMBER</b> (8/12) millions of ft.                   | 438.7#      | 435.1     | -8.2         |
| <b>RAIL FREIGHT</b> (8/12) billions of ton-miles       | 24.2#       | 23.6      | 0.8          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWP, SFPA, Association of American Railroads

## PRICES

|                                                           | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|-----------------------------------------------------------|-------------|----------|--------------|
| <b>GOLD</b> (8/23) \$/troy oz.                            | 382.750     | 382.000  | 0.2          |
| <b>STEEL SCRAP</b> (8/22) #1 heavy, \$/ton                | 146.50      | 146.50   | 8.9          |
| <b>COPPER</b> (8/18) ¢/lb.                                | 143.4       | 140.1    | 27.0         |
| <b>ALUMINUM</b> (8/18) ¢/lb.                              | 88.8        | 88.5     | 25.0         |
| <b>COTTON</b> (8/18) strict low middling 1-1/16 in, ¢/lb. | 84.99       | 81.68    | 24.9         |
| <b>OIL</b> (8/22) \$/bbl.                                 | 18.54       | 17.42    | 5.9          |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                               | LATEST WEEK | WEEK AGO | YEAR AGO |
|-------------------------------|-------------|----------|----------|
| <b>JAPANESE YEN</b> (8/23)    | 96.36       | 97.75    | 99.36    |
| <b>GERMAN MARK</b> (8/23)     | 1.48        | 1.48     | 1.54     |
| <b>BRITISH POUND</b> (8/23)   | 1.54        | 1.55     | 1.56     |
| <b>FRENCH FRANC</b> (8/23)    | 5.07        | 5.06     | 5.29     |
| <b>ITALIAN LIRA</b> (8/23)    | 1617.5      | 1623.5   | 1571.3   |
| <b>CANADIAN DOLLAR</b> (8/23) | 1.36        | 1.36     | 1.37     |
| <b>MEXICAN PESO</b> (8/23)    | 6.270       | 6.165    | 3.355    |

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

## EMPLOYMENT

Friday, Sept. 1, 8:30 a.m. ▶ The MMS median forecast is that nonfarm payrolls grew by 155,000 in August, after just 55,000 jobs were added in July. The August unemployment rate likely rose to 5.7%, from 5.6%.

## CONSTRUCTION SPENDING

Friday, Sept. 1, 8:30 a.m. ▶ Building outlays probably rose 0.5% in July, says the MMS report. Spending in June jumped 0.9%.

## NAPM SURVEY

Friday, Sept. 1, 10 a.m. ▶ The National Association of Purchasing Management's business index probably stood at 51.5% in August, up from 50.5% in July.



# This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

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## Sunday

Talk about the Cover Story on 3-D computing with Dan Mapes of SynergyLabs (his special-effects magic is on view in the sci-fi movie *Virtuosity*) and Business Week's Peter Coy. **Aug. 27 9 p.m. EDT in the Globe**

## Thursday

What kind of economy can we expect this fall? Who better to ask than James Cooper and Kathleen Madigan of BW's closely watched Business Outlook? **Aug. 31 9 p.m. EDT in the Globe**

## Downloads

Transcripts of all conferences are available for downloading from the BW Online area of AOL, under Search BW. Try these recent standouts:

- Making the Most of Win95
- Investing in High Tech
- Disney's Kingdom

## Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

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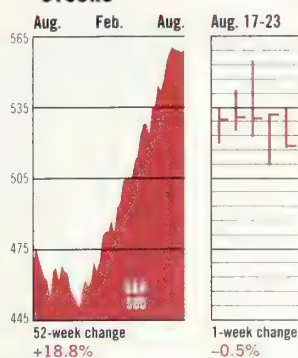
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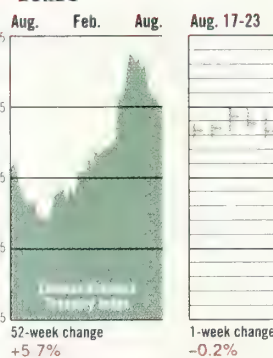
## MARY

week for U.S. blue-chip  
generally trading  
of the week, the Dow  
trial average fell 36  
585, on Aug. 23. The  
ded Microsoft Corp.,  
due to concerns about  
i. But strength among  
ology stocks sustained  
ndex. Bonds declined,  
use of weak demand at  
of five-year notes. The  
ned from its recent  
y because of an expect-  
Germany would cut

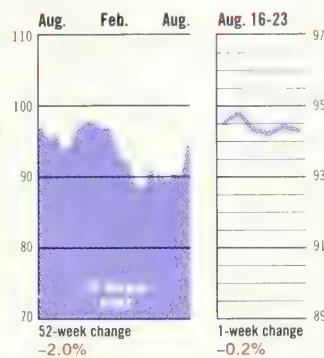
## STOCKS



## BONDS



## THE DOLLAR



## MARKET ANALYSIS

### MARKS

|                            | Latest | % change |         |
|----------------------------|--------|----------|---------|
|                            |        | Week     | 52-week |
| INDUSTRIALS                | 4584.9 | -1.2     | 19.2    |
| MPANIES (S&P MidCap Index) | 210.4  | 0.5      | 19.7    |
| PANIES (Russell 2000)      | 304.5  | 0.7      | 20.5    |
| VIES (Russell 3000)        | 321.5  | -0.3     | 19.3    |

### STOCKS

|                    | Latest   | % change (local currency) |         |
|--------------------|----------|---------------------------|---------|
|                    |          | Week                      | 52-week |
| NANCIAL TIMES 100) | 3515.9   | 1.5                       | 9.7     |
| (EI INDEX)         | 17,732.0 | -2.4                      | -13.6   |
| SE COMPOSITE)      | 4608.0   | 0.0                       | 8.1     |

### FUNDAMENTALS

|                              | Latest | Week ago | Year ago |
|------------------------------|--------|----------|----------|
| 90-DAY TREASURY BILL YIELD   | 5.59%  | 5.57%    | 4.63%    |
| 30-YEAR TREASURY BOND YIELD  | 6.91%  | 6.88%    | 7.46%    |
| S&P 500 DIVIDEND YIELD       | 2.42%  | 2.39%    | 2.71%    |
| S&P 500 PRICE/EARNINGS RATIO | 16.0   | 16.2     | 18.7     |

### TECHNICAL INDICATORS

|                                           | Latest | Week ago | Reading  |
|-------------------------------------------|--------|----------|----------|
| S&P 500 200-day moving average            | 504.3  | 502.0    | Positive |
| Stocks above 200-day moving average       | 75.0%  | 74.0%    | Negative |
| Speculative sentiment: Put/call ratio     | 0.54   | 0.60     | Negative |
| Insider sentiment: Vickers sell/buy ratio | 2.31   | 2.29     | Neutral  |

BLOOMBERG FINANCIAL MARKETS

## TRY GROUPS

### TH LEADERS

|                    | % change |          | Strongest stock in group | % change |          | Price   |
|--------------------|----------|----------|--------------------------|----------|----------|---------|
|                    | 1-month  | 12-month |                          | 1-month  | 12-month |         |
| CARE SERVICES      | 14.9     | 32.0     | AMGEN                    | 20.6     | 75.5     | 48 1/4  |
| TIME               | 10.0     | 5.1      | BRUNSWICK                | 14.1     | -1.2     | 21 1/4  |
| ASTING             | 9.9      | 26.5     | CAPITAL CITIES/ABC       | 14.9     | 47.6     | 116 3/4 |
| ICATIONS EQUIPMENT | 9.8      | 73.6     | CISCO SYSTEMS            | 23.9     | 187.0    | 66      |
| ORTATION SERVICES  | 8.9      | 0.3      | FEDERAL EXPRESS          | 14.9     | 7.6      | 74 1/8  |

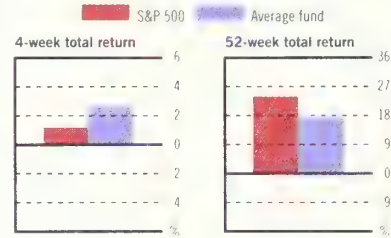
### TH LAGGARDS

|                      | % change |          | Weakest stock in group | % change |          | Price  |
|----------------------|----------|----------|------------------------|----------|----------|--------|
|                      | 1-month  | 12-month |                        | 1-month  | 12-month |        |
| TY APPAREL RETAILERS | -11.6    | -17.2    | THE LIMITED            | -13.8    | -3.9     | 18 3/4 |
| ND GLASS CONTAINERS  | -7.2     | 22.8     | CROWN CORK & SEAL      | -7.5     | 21.8     | 43 1/4 |
| MERCHANDISE CHAINS   | -5.9     | 9.2      | WAL-MART STORES        | -7.7     | 5.7      | 25 3/8 |
| AINS                 | -4.4     | 27.9     | WALGREEN               | -4.9     | 29.4     | 24 1/2 |
| TIONAL OIL           | -4.1     | 12.6     | EXXON                  | -6.3     | 15.8     | 68 1/8 |

## L FUNDS

MORNINGSTAR INC

|                              |       | LAGGARDS                            |       |
|------------------------------|-------|-------------------------------------|-------|
| total return                 | %     | Four-week total return              | %     |
| APITAL APPRECIATION          | 12.9  | COLONIAL NEWPORT TIGER Z            | -5.2  |
| PRICE SCIENCE & TECHNOLOGY   | 12.8  | VAN ECK ASIA DYNASTY B              | -5.1  |
| DVISORS INNOVATION A         | 12.3  | WRIGHT EQUIFUND-BELGIUM/LUXEMBOURG  | -5.0  |
| tal return                   | %     | 52-week total return                | %     |
| N COMMUNICATIONS & INFORM. A | 109.4 | WRIGHT EQUIFUND-MEXICO              | -48.7 |
| APITAL APPRECIATION          | 98.9  | BT INVESTMENT LATIN AMERICAN EQUITY | -35.1 |
| SMALLER COMPANIES A          | 95.5  | TCW/DW LATIN AMERICAN GROWTH        | -34.5 |



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as indicate  
tal returns



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+0.17%



Treasury bonds  
**\$11,647**  
+0.48%



Foreign stocks  
**\$10,828**  
+0.25%



Money market fund  
**\$10,532**  
+0.12%



Gold  
**\$10,194**  
+0.12%

s page are as of market close Wednesday, Aug. 23, 1995, unless otherwise indicat-  
roups include S&P 500 companies only; performance and share prices are as of mar-

ket close Aug. 22. Mutual fund returns are as of Aug. 18. Relative portfolios are valued as of Aug.  
22. A more detailed explanation of this page is available on request. r=revised NA=Not available



## WHAT THE U.S. CAN DO ABOUT TAIWAN

Should the U.S. start worrying about the prospect of armed conflict between China and Taiwan? After almost a decade of relative peace, China is conducting military exercises just 95 miles from Taiwan, including test-firing missiles and practicing blockade maneuvers. The objective? To influence Taiwan's first-ever direct presidential elections, to be held next March, and dissuade Taiwan from edging toward formal independence. This raises the appalling possibility of ever-escalating military tensions between two countries that are both strategically and economically critical for the U.S.

Since the 1970s, the U.S. has maintained a "one-China" policy, which is based on the diplomatic fiction that the mainland and Taiwan are both part of the same country, while unofficially keeping up economic and security ties to Taiwan. But both China and Taiwan have changed dramatically in the decades since the policy was formed. Taiwan has become an economic powerhouse and a main supplier of electronic components to the U.S. Politically, the country has been steadily moving from being a brutal dictatorship to a full democracy led by a new generation of Taiwan-born politicians, such as current President Lee Teng-hui, who are more interested in gaining international recognition than in working toward reunification with the mainland. At the same time, China has moved from basket case to budding superpower: It has pumped up both its economy and its armed forces enough to be confident of its ability to mount an effective blockade of Taiwan.

Over the long run, the U.S. needs to conduct a high-level policy review to reassess and perhaps update its one-China policy. Right now, however, is not the time to be making dra-

matic changes in longstanding policies. Because of the taints of the coming succession in Beijing, the Chinese leadership is exceptionally unwilling to show signs of weakness. Not even the moderates in Beijing want to be seen as abandoning Taiwan.

For now, the U.S. must move carefully. It must have priority on buttressing the status quo, which has helped both the Taiwanese and Chinese to prosper. The Clinton administration and Congress can't simply bury their heads in the sand and hope this conflict will fade away. Despite the immediate appeal of a Taiwan legally separate from China, the U.S. can't afford to egg on pro-independence Taiwanese politicians by giving them false hopes that it would defer to them against a Chinese invasion. That means, for example, discouraging Taiwan from applying for membership in the United Nations, a move sure to inflame China.

At the same time, the U.S. must send a clear and unambiguous message to the Chinese that it's totally unacceptable to use military power to intimidate a neighbor. Hillary Clinton should cancel her trip to Beijing for the upcoming U.N. Conference on Women to show Washington's approval of both China's saber-rattling and its treatment of human rights activist Harry Wu. And President Clinton should ask former President George Bush to defer his scheduled trip to China as well. Additional actions may be needed at a time when Boeing, Ford, Lockheed Martin and other companies are making major new sales in China. But the U.S. needs a politically stable Asia even more than it needs market access.

## BREAST IMPLANTS: THE EVIDENCE ISN'T IN

Just as the O.J. Simpson case has become the benchmark for how not to conduct a murder trial, so too is the battle over silicone breast implants well on its way to setting new lows for product-liability cases. On one side are almost half a million women who claim they were or could be harmed. On the other side are the implant manufacturers, including Dow Corning Corp. and Bristol-Myers Squibb Co., which face the possibility of enormous damages. A \$4.2 billion settlement—the largest in litigation history—negotiated a year ago to settle a class action was supposed to avoid ruinous and protracted legal proceedings. But it has broken down, and there's little hope for a new agreement by the Aug. 30 deadline set by the judge.

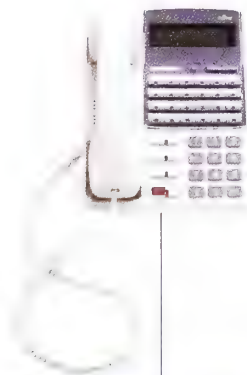
One thing making it hard to reach an agreement is the inconclusiveness of the scientific evidence presented so far. Recent studies show no link between implants and typical autoimmune diseases that implants were originally suspected of causing, such as rheumatoid arthritis and lupus. But women with implants may suffer from other diseases as well, and doctors are often slow to recognize problems that don't fit con-

ventional categories. For example, many of the recently covered tick-borne illnesses may have been around while without being noticed by the medical profession.

Fortunately, more answers may be coming. Scientists at Brigham & Women's Hospital in Boston are nearing the completion of a huge study of 450,000 women (of whom about 9,000 have implants) that examines atypical symptoms as well as traditional suspects. When the study is finished in early 1997, it will be attacked by whichever side doesn't like its conclusions. But however imperfect, this research and other studies offer hope for finding out how risky silicone breast implants are—and how much compensation women deserve.

With new evidence on the way, the Aug. 30 deadline is soon. Rather than rushing plaintiffs and defendants to a settlement that may fall apart again, the judge should give them more time. As one scientist observes: "The search for scientific truth should precede all the litigation and fighting. It may not be what litigious America chooses, but relying on the best science available is the preferred alternative in the long run."

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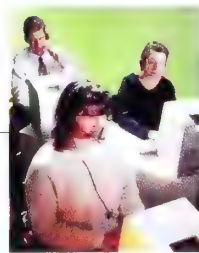
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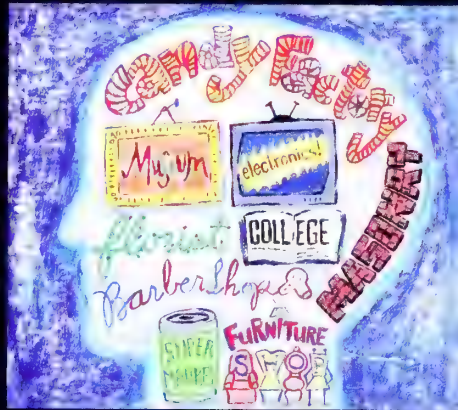
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# THE RACE FOR BIGNESS

The megamergers keep coming.  
**Chemical** and **Chase** join (\$10 billion deal) to become the largest U.S. bank.



Gerald Levin  
CEO  
Time Warner

**Time Warner** goes after  
**Turner** (\$8 billion) to stay  
on top in entertainment.



Walter Shipley  
CEO-Designate  
Chase Manhattan

The **Disney-ABC** deal (\$19 billion) isn't even closed. Name the industry—drugs, utilities, railroads—and it's the same story. Why is all this happening

...and where will it lead?

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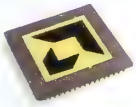
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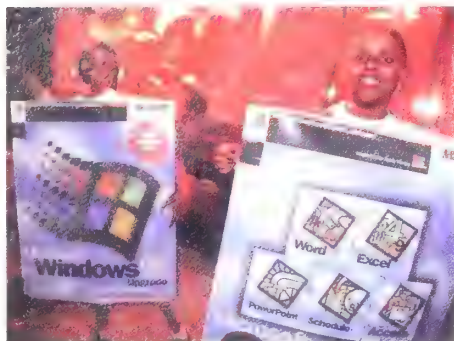
Bigger, sure. Better? Well...

Emerging markets can be a snake pit



# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI



**HOOPLA:** The Win95 rollout

## SOFTWARE HARDBALL

### JUSTICE PEERS AT WINDOWS 95

WIN95 HAS AN UNSOCIABLE side that may give the Justice Dept. some ammo for its continuing antitrust probe of Microsoft. The problem is that Win95 sometimes disrupts rival products' Internet links. Occasionally, it destroys Net-connecting programs, such as Quarterdeck Internet Suite. Many consumers who bought the much-ballyhooed new Microsoft program are complaining about this.

## CAPITAL OFFENSES

### THE AIDE THAT WOULDN'T LEAVE



**SHUSTER:** Loyal pal

IT'S THE SAME old Washington revolving door. The former top aide of House Transportation Committee Chairman Bud Shuster (R-Pa.) lobbies the panel—and helps run his reelection campaign. Ann Eppard, his \$108,000-a-year chief of staff until last November, falls afoul of no law. Federal conflict-of-interest statutes ban highly paid ex-Hill staffers from lobbying former bosses. Eppard says she lobbies members of the commit-

The Justice Dept. is looking into competitors' claims that Windows 95 is designed to deprive other players of a level playing field. In early August, Justice backed off from seeking an injunction to stop the Windows 95 debut, but it still fears the new Microsoft Network built into the program will end up dominating other online services. David Pool, executive vice-president of CompuServe's Internet arm, grouches that Microsoft has withheld the info needed to make Win95 dial easily into non-MSN Internet providers.

Microsoft Chairman Bill Gates denies it has kept data from CompuServe. Microsoft says that it is working to fix blocked links between other Internet products and Win95. *Stephen H. Wildstrom*

tee, never the chairman.

After helping shape federal transportation policy for 25 years, she opened Ann Eppard Associates and enlisted such clients as Amtrak, Conrail, and the Pennsylvania Turnpike Commission. As of July 20, her company has raked in more than \$200,000 in fees. "She advises us on how to structure our arguments," says a spokesman for the American Road & Transportation Builders Assn. Meanwhile, she has identified herself in correspondence as assistant treasurer of Shuster's reelection group.

In a May interview, Eppard argued that her work is typical of former Hill staffers. This week, neither she nor Shuster returned numerous calls. *Christina Del Valle*

**TALK SHOW** "The ads' message about the spirit, independence, and inner worth of today's young people have been misunderstood by some..."

—Calvin Klein company statement as it withdrew jeans ads with teens in suggestive poses

## RACKET SQUAD

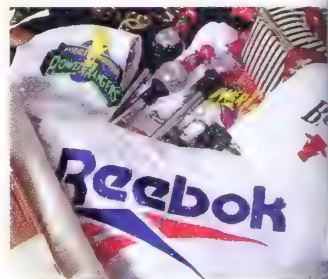
### OUT! OUT! DAMNED KNOCKOFFS

SELLING COUNTERFEIT GOODS is a booming—and blatant—business. U.S. manufacturers fume that worldwide losses from bogus goods have ballooned to \$200 billion a year, up from \$5.5 billion in 1982. Reason: The cops prefer to chase drug dealers and murderers. So peddlers sell pirated movie videos right in front of the U.S. Patent & Trademark Office in Washington.

But there's a crack-down in one spot. The Manhattan District Attorney's office is seeking to evict knockoff artists from a major distribution center, a five-story building at 1165 Broadway, near 27th Street, where officials say wholesalers flock to collect fake merchandise. Previous raids have failed to stop counterfeiters, who simply open up shop in another part of the building, which also contains legitimate distributors.

With the help of 1165's landlord, Sam Haddad, the D.A.'s office is suing to

throw out alleged counterfeiters under New York's "bawdy-house law," enacted in the 19th century to drive prostitutes. Two tenants agreed to leave, and others could face eviction if they don't settle, says lawyer, Peter Verby. But more have filed a motion to dismiss their cases, and



**HAUL OF SHAME:** Counterfeit

that the bawdy-house law applies only to vice crimes. Timized companies, including Guess Jeans and Ralph Lauren, hope other cities can't use statutes to attack knockoff havens such as those on Tees Alley in Los Angeles or Buford Highway outside Atlanta. *Catherine*

## THE LIST LOSE SOME, WIN SOME

The Chemical-Chase merger may mean the loss of 4,000 jobs for metropolitan New York, where the workforce has been shrinking since the



1980s. But the New York region also boasts the largest number of companies with expanding payrolls. Example: new multimedia startups in Lower Manhattan. The San Francisco area, home to Silicon Valley, is No. 2. Los Angeles' booming entertainment industry is hiring, too.

## JOB-GENERATING COMPANIES

| METRO AREA             | NO. OF COMPANIES |
|------------------------|------------------|
| 1 NEW YORK             |                  |
| 2 SAN FRANCISCO        |                  |
| 3 LOS ANGELES          |                  |
| 4 BOSTON               |                  |
| 5 DALLAS-FORT WORTH    |                  |
| 6 CHICAGO              |                  |
| 7 HOUSTON              |                  |
| 8 MINNEAPOLIS-ST. PAUL |                  |
| 9 PHILADELPHIA         |                  |
| 10 ATLANTA             |                  |

\* During most recently ended fiscal year. Inclusion, company must have at least 1 payroll growth and 100 to 499 employees, and 500 to 999; or 5% and 1,000 or more. DATA: HOOVER'S MASTERLIST DATABASE. THE REFERENCE PRESS INC.



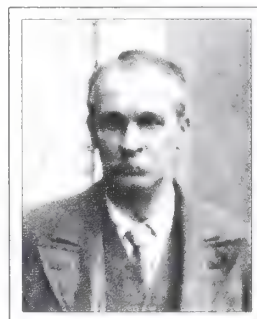
The Cup is a biennial competition that brings together the finest professionals from both sides of the Atlantic in three days of tension-filled match play competition. In continuing testimony to the noble heritage



*Oak Hill Country Club, site of the 1995 Ryder Cup*

of golf, the Ryder Cup is contested not for money, but for the far greater reward of bringing home one of golf's most treasured trophies.

Underwritten in 1927 by English seed merchant Samuel Ryder, the Cup is hosted in the U.S. by the PGA of America,



*Samuel Ryder was a generous sponsor of professional golf and donor of the gold trophy, the Ryder Cup*

## Rolex and the Ryder Cup. Well teamed.

In Kiawah, South Carolina, in 1991, it came down to a six-foot putt on the final hole of the final match. Two years later at The Belfry in Sutton Coldfield, England, the outcome was decided by a three-footer on the penultimate hole. In both cases, the American Team emerged with the narrowest of victories over their illustrious European counterparts; but the real winners were the millions of fans all over the globe, and the Ryder Cup itself, which is now widely recognized as one of the most stirring events in all of golf.



which also conducts the PGA Championship, the PGA Seniors' Championship, and the PGA Grand Slam of Golf.

When play begins in the 1995 Ryder Cup Matches at the Oak Hill Country Club in Rochester, New York, this September, all timing functions will be carried out by a timepiece with its own proud history of dramatic performance. Rolex. The Official Timepiece of the PGA of America.



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# Up Front

## FOREIGN INTRIGUE

### GE BRINGS IFFY THINGS TO LIGHT



**CAT SCAM?** *Gear never got used*

GENERAL ELECTRIC, MADE bold by the Italian authorities' Clean Hands probes, has won a suit against a Palermo hospital that it alleges illegally awarded a contract to a competitor. This is one of the first signs that the government's anticorruption campaign is taking hold in Italy, where unethical business practices have long been shrugged off.

At issue here is a CAT-scan device that GE sought to sell to Ospedale Cervello di Palermo in 1987 for about \$940,000. Instead, the hospital bought the machine from Tecnologie Medicali, the Italian agent for New Elscint Technologies, an Israeli company. GE says it will

seek to collect around \$200,000 in damages from New Elscint, claiming that the Israeli machine didn't meet the hospital's specifications. The hospital denies that. Neither the agent nor New Elscint could be reached.

Bolstering GE's case is the three-year-old Clean Hands drive. Prosecutors are alleging there is wrongdoing at

## DRAWN & QUARTERED



the hospital. Six of its doctors and two Tecnologie Medicali employees have been arrested on kickback charges; they couldn't be reached for comment. The alleged scheme: The CAT scan was never used, and patients went for tests to private clinics, which paid the doctors \$375 per visit. Clean Hands has resulted in scores of corruption charges against judges, politicians, and business magnates. *Christina Bennett*

## PRODUCT PEEK

### IT PAYS TO PUFF IN BRITAIN

SMOKERS FINALLY break. Britons can now get an annuity paying a higher return than common ones if they have smoked cigarettes daily for the last decade. Stalwart, a life insurer, apparently believes smokers' higher

## CAPITAL IDEAS

### CAN SEVIN ROSEN WIN SANS ROSEN?



**ROSEN:** *Home run hitter*

THE TORCH IS being passed at high-flying venture-capital outfit Sevin Rosen Management. Its newest fund, \$100 million Sevin Rosen V, will be its first without Benjamin Rosen, the former Wall Street analyst-

turned-venture-marvel, as a partner. Rosen, who remains an adviser to the company, is spending more time on an electric-car start-up. "I'm completing the phase-down," says Rosen, 63.

The Dallas company's first fund, raised in 1981, is considered one of the biggest home runs in high-tech investing. General partners Rosen and semiconductor guru L.J. Sevin backed such blockbusters as Compaq Computer, Lotus Development, Cypress

Semiconductor, and Silicon Graphics. The fund's \$2.5 million 1982 investment in Compaq is now worth \$1.1 billion.

General partners heading the newest fund will be five Young Turks from Sevin Rosen. They're sticking close to the Sevin Rosen investment philosophy, focusing Fund V on making seed and early-stage investments in information technologies such as communications, semiconductors,

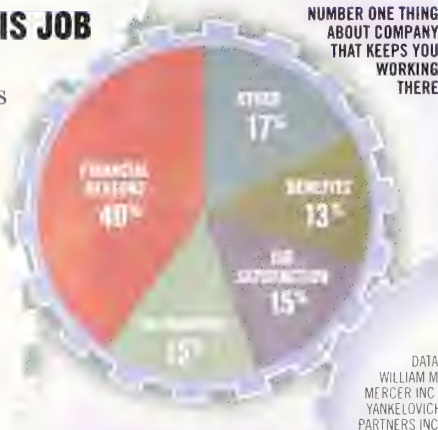
and software, says general partner John Jagers.

One change: the younger generation's interest in biotech. Fund V will invest in life-science startups, which Sevin Rosen first explored in Fund IV with such investments as ArQule, maker of chemical building blocks for drugmakers. But it's too soon to assess that bet: None of the Fund IV outfits has gone public. *Gary McWilliams*

## THE BIG PICTURE

### WHY I DO THIS JOB

Not surprisingly, their paycheck is the main reason people work where they do. But don't underestimate other factors. Most people say the critical element in a job is something other than take-home pay.



mortality rates mean they have to pay for fewer years. Smokers don't even have to keep puffing to stay eligible. Ghoulis? Stalwart Managing Director Mike Fuller, in a statement only for smokers would have "a standard of living," that is, richer payouts. While some are rich about the notion, Norwich Union Insurance Group and other giants admit they have to follow suit if a winner. The contrast is compelling. With Stalwart's 60-year-old male smoker pays \$77,000 would get \$77,000 yearly. Norwich, like other insurers, makes no distinction between smoking and non-smoking annuitants. Norwich payout: \$7,672. *Robinson*

**FOOTNOTES** Bullish on the market: women, 40%; men, 48%. Bearish: women, 7%; men, 20%

chipmunk: 1.3 years.

butterfly: 2 weeks.

toad: 21 days.

chickadee: 6-7 years.

mayfly: 48 days.

goldfish: 7 years.



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## DISNEY & CO. DRIVING THE ECONOMY? THAT'S GOOFY

Wall Street megadeals, like those that saw Walt Disney merge with Capital Cities/ABC and Westinghouse Electric purchase CBS, still seem to have the power to propel the business press toward flights of fantasy. How else to explain your recent editorial insisting that entertainment has become "the driving force of the U.S. economy" ("The expanding entertainment universe," Editorials, Aug. 14). Despite the well-publicized downsizing of some large industrial companies, manufacturing remains the true engine of American economic growth.

U.S. economic prowess has been built on high productivity, low inflation, and booming exports—all areas where the manufacturing sector, not entertainment, excels. Manufacturing productivity grew by an average of 2.4% from 1985 to 1993, six times the productivity growth elsewhere in the economy. Meanwhile, prices of manufactured goods have risen an average of only 2.4% a year since 1981, half the rate of services. And in the past five years, exports of U.S. manufactured goods grew at an average annual rate of more than 10%.

Mickey, Minnie, and Goofy may be worthy ambassadors for American entertainment, but when it comes to representing overall economic power, they take a backseat to computers, semiconductors, and aircraft.

Jerry J. Jasinowski  
 President  
 National Association  
 of Manufacturers  
 Washington

## ALL ABOARD FOR MACHU PICCHU

It was a pleasure to read Bob Dowling's "Machu Picchu: A magical mystery tour" (Personal Business, Aug. 21). The recovery of tourism activity in Peru, not only for archaeological and historical attractions but for a variety of ecological and nature tours, reflects the new pre-

## CORRECTIONS & CLARIFICATIONS

"Glitches in the system at DEC" (Information Processing, Aug. 21) overstated DEC Equipment Corp.'s prior PC growth rate. It should have said the company's world PC ranking as of July 1 remained steady at 11th place. In addition, the story should have noted that three national PC chains sell its products, all of which were signed up by the group's former president.

In describing a suit filed by Ohio's Cuyahoga County against seven securities firms ("Cuyahoga County vs. the Street" (Business This Week, Aug. 28) implied PaineWebber Inc., a defendant, had declined to comment on the case. In fact, PaineWebber told BUSINESS WEEK that the transactions cited by Cuyahoga were not securities of Kidder Peabody Group Inc., which acquired from General Electric. PaineWebber says that those liabilities remain with GE and that it expects to be moved as a defendant in the suit.

In "The drought won't lift" (Business Outlook, July 31), the estimate for bad loans in Japan each year is 2 trillion to 5 trillion yen.

In "Easing your way onto the Net" (Technology & You, July 24), the price for Finance System International's Internet service should have been \$9 a month.

Incident involving security conditions. Incidents involving the State Dept. decided on July 21 to remove the travel warning for Peru mentioned in light of the positive results Peru has accomplished in recent months. Ricardo Valdivia  
 Ambassador of Peru  
 Washington

## REVLON'S ALLURE MAY DEPEND ON PERELMAN

Your article about Ron Perelman's empire ("The Operator," Cover, Aug. 21) illustrates the difficulty of putting a value on a privately held company. The method used by BUSINESS WEEK

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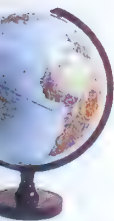


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twelve  
time zones  
hold up  
our 9:00 meeting?

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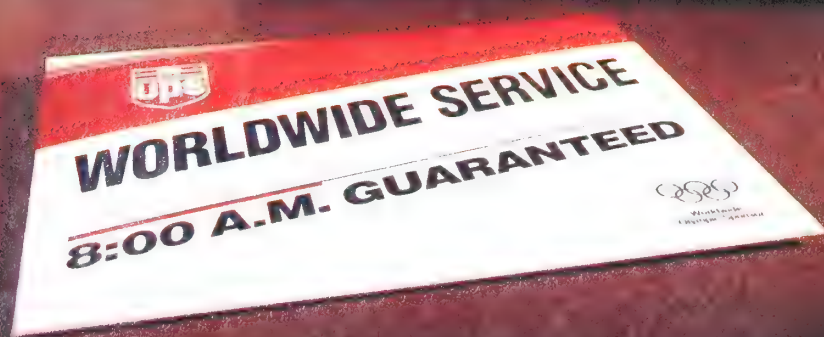
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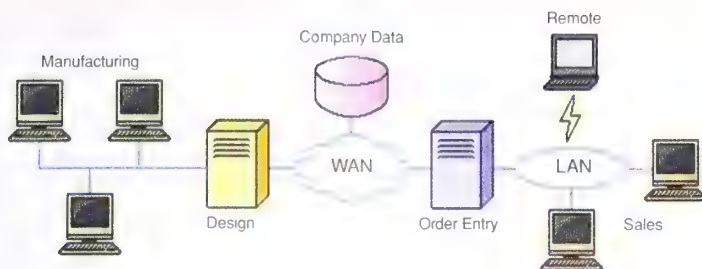


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# Readers Report

far more accurate than the method of Perelman's associates, may also overstate the value of Perelman's holdings.

Ironically, the biggest negative may be Perelman's own considerable management skills. A given in a public offering is that his eye and his interest would begin to move elsewhere. The company may not perform as well with his operating talents removed. That factor alone may lower the value by 10% to 30%. At a 30% discount, Revlon actually has no net worth. This, along with the other factors mentioned, accounts for the inability to get an initial public offering done in 1992 and could cause the same difficulty in 1996.

Tim Raetzloff  
Edmonds, Wash.

## PART-TIME B-SCHOOL: PRIDE AND PROTEST

With four children and a mortgage, I knew that studying for an MBA part-time at Indiana University was my only option ("Part-time B-School is a full-time grind," *Personal Business*, Aug. 21). From 1968 to 1972, as part of a

### B-SCHOOL BLUES

"Unless you can afford the time, money, and effort... at Harvard, Stanford, Wharton, Northwestern, or Chicago, you're wasting your time"

group of seven employees from Cummins Engine Co. and Arvin Industries Inc., I carpooled a total of 26,000 miles back and forth from Columbus, Ind., to Bloomington and Indianapolis to complete night-school MBAs. We had the same excellent classes and professors as the full-time students. We did miss the interaction with other students and professors outside of classes. But we formed class-project teams within our carpool group.

It's true there is no salary change or promotion upon completion of a part-time MBA. This is because the salary increases and promotions were continuous throughout our careers rather than at MS or MBA completion milestones.

Joseph J. Neff  
Indianapolis

One of the biggest problems that is faced by part-time business-school programs is they do not carry the name

recognition of the full-time programs. However, I feel that the MBA I recently earned from the Keller Graduate School of Management was well worth the sleep deprivation and the price paid. The program provided me with a tremendous boost in self-confidence, the tools necessary to compete in a dynamic marketplace, and an education that is directly applicable to life in general. That is a payback far more worthwhile than what I might have received at another school—one perhaps better known for its football team than its business school.

Theodore L. Coddington  
Phoenix

Not only is part-time B-School a full-time grind, it is often counterproductive in enhancing a person's career prospects. Unless you can afford the time, money, and effort (and can get accepted) at Harvard, Stanford, Wharton, Northwestern, or Chicago, you're wasting your time with a lesser MBA program. While the very top schools continue to command respect and high salaries from

employers (in part because of their selectivity), quite often it does more harm than good to earn an MBA from a lightly regarded institution.

In today's competitive work environment, the vast majority of middle managers are too busy to

pursue a part-time MBA. Frequently, those who do so see their work performance suffer—with predictable results for their career. Some employers, correctly or not, view an MBA from an undistinguished institution as representing a candidate's interest in taking on staff assignments as opposed to line positions, which are, of course, the real work of most businesses. Longtime headhunters, like myself, know that any undergraduate degree provides a significant advantage for your career. The parallel argument cannot be made for MBA programs.

Bert L. Kizer  
Hinsdale, Ill.

## MOTOROLA MISSED AT LEAST ONE S.O.S.

In "Motorola's school for parents" (*Up Front*, Aug. 21), Kevin Kelly reports that Motorola has mailed out

copies of its recently researched let, *The Role of the Adult in the of a Child*. As the wife of an ex at Motorola, I find that the cor jump onto the bandwagon too late.

In the past six years, Motorola sued similar booklets on educat the drug problem. Interestingly over the last few years I have v my own family disintegrate as of a workaholic husband. (Our lastion from work and the childr 1976.) All of my pleas for help to the Motorola Employee Assistan gram have gone unheeded. What about "40 hours of job-related yearly"? Not my husband—he have to leave his work. I'm now with an impending divorce aftering stood by my husband and for 26 years.

Thank you, Motorola, for encouraging your executives to spend time with their families and to take a break away from work. (It's vacation, I think.)

Elizabeth Anne  
Austin, Tex.

## A GRISLY PHOTOGRAPH THAT'S BEYOND THE PALE

Your article, "Russia's really takeovers" (*International Business Week*, Aug. 14), includes a grisly close-up of a man face down with a bullet through his head. The death of a man is unfortunate. And *BUSINESS WEEK*'s exploitation of his death is offensive.

Karen  
Los Angeles

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## TRUST

The Social Virtues and the Creation of Prosperity

By Francis Fukuyama

Free Press • 457pp • \$25

# WHEN SELFISHNESS DOESN'T PAY OFF

Francis Fukuyama is not one to shy away from the big issues. In his 1992 book, *The End of History and the Last Man*, he argued that the cold war's end had allowed the emergence of a global consensus in which liberal democracy and a market economy were seen as the only viable approaches to organizing society. Critics assailed him for brushing aside such issues as militant Islam and ethnic turmoil in the old Soviet bloc. Yet the book clearly helped shape the debate on how the world would evolve after communism's collapse.

Fukuyama, a senior social scientist at Rand Corp., has now come out with *Trust: The Social Virtues and the Creation of Prosperity*, a kind of sequel to his earlier work. In it, Fukuyama tries to predict what kind of societies will flourish in this new, free-market world. The result is an intriguing work with a number of flaws, including a ponderous style and many hard-to-follow arguments. But this book, like his last, will generate plenty of discussion because it tackles the hot topic of social capital—the idea that a healthy community life is essential to prosperity.

Fukuyama's thesis goes like this: Economists have focused far too much on the idea that the rational, selfish behavior of humans in the marketplace best explains the rise and fall of societies. To get a complete picture of how society works, they should consider such "arational" factors as religion, tradition, and the concepts of honor and loyalty. How a society approaches these parts of communal life dictates how much trust exists among its members.

The higher the level of trust, the more there is of what Fukuyama calls "spontaneous sociability." That's the willingness of a society's members to join organizations—such as sports societies, charitable organizations, new religious groups, or political clubs—that lie outside the family. Such sociability, in turn, prepares people psychologically for working cooperatively in large, private companies, which Fukuyama says can amass capital and develop key technolo-

gies much more efficiently than small, family-run ventures.

Using these schemata, Fukuyama then takes the reader on an exhausting tour of low-trust and high-trust societies. The results include some interesting comparisons. He identifies China, Italy, and France as low-trust societies and puts Germany, the U.S., and Japan in the high-trust category.

Low-trust societies, he says, can produce plenty of successful family-run companies. But they face a struggle moving up to the next rung of economic activity, where much larger, private companies flourish without any need of state subsidies. The reasons for this vary. In China, Confucianism encouraged the organization of society around the family and clan—institutions that Maoist communism failed to destroy. These families tend not to trust nonmembers, thus making larger cooperation impossible. And the flaw can extend to the overseas Chinese as well—just look at the experience of Wang Laboratories in the U.S., says the author. Company founder An Wang doomed the once-illustrious computer maker by giving huge management responsibility to his unprepared eldest son. Likewise, in poverty-stricken Southern Italy, suspicion of outsiders makes large-scale economic cooperation impossible. (He admits Northern Italy is a different case but still labels the country a low-trust society.) In France, royal absolutism demolished independent associations such as guilds and imposed an intrusive bureaucracy that weakened entrepreneurialism and used the state to prop up ailing corporations.

The connections Fukuyama draws between Germany, the U.S., and Japan are just as clever. In Germany, the persistence of the guild tradition into the 19th century produced quality-conscious

workers whom managers could. In the U.S., the absence of a strong religion allowed Protestant churches to multiply easily by recruiting new members, who acquired the habit of all kinds of associations, including fraternities. In Japan, the tradition of *iemoto*—hierarchical, voluntary associations that pursue activities such as archery or flower-arranging—prepared people for life inside big corporations and the *keiretsu*.

There are lots more such examples and arguments. Fukuyama also notes that America's other tradition, individualism, now poses a threat to sociability. In the U.S., he says, "communities of shared values... have become rarer. And it is these moral communities alone that can generate the social trust that is critical to organizational efficiency."

The above quote illustrates *Trust's* serious flaws: The prose is mighty dry, even when discussing an urgent matter of a nation's moral health. Another problem is the book's

Do we really re- such a minutely d history of the *keiretsu* of the ins and o German craft-apprentiship law?

Worse, the book lightly over certain issues. One ex Germany has flour as a high-trust s But now, big G employers, fed up the costs of the G welfare state, are up operations in low-cost countries China, India, and I

That's a major sign of distrust in a high-trust system. Likewise, Japan's crisis was created partly because society distrusts outsiders and protectionist trade. Fukuyama goes on to both predicaments but doesn't really address them. Finally, Fukuyama doesn't really say if low-trust societies can actually turn themselves into high-trust societies. He confines himself to a warning that societies should not dismantle or ignore religion and traditional ethics, which are the wellsprings of social health.

There's plenty to argue over in Fukuyama's book. But he's got the theme right. Societies need social capital. The end of history or no.

BY CHRISTOPHER L. CLARK  
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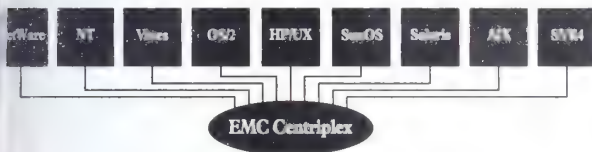


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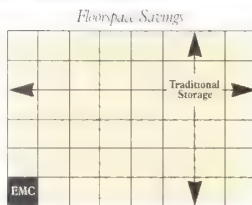
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BY STEPHEN H. WILDSTROM

## FEELING YOUR WAY AROUND THE WEB

If you are one of the millions of people who have become World Wide Web explorers in the past few months, undoubtedly you've discovered some odd and interesting sites, often purely by chance. But don't you wonder whether there's a better way to find what you want? The answer is a resounding "yes." The trick is to learn how to use some tools that will richly reward a little patience and persistence.

Looking for information on the Web is a little like browsing in a library, where the card catalog is your guide. Search tools, the catalogs of the Web (table), come in two basic flavors. Directories, such as Yahoo, are lists of Web sites classified by topic. Indexes, such as Lycos, allow you to find specific documents through keyword searches. **"DRILL DOWN."** A directory is most useful when you are interested in a general subject but don't know exactly what you want. Yahoo, a former academic service that is now supported by fairly unobtrusive on-screen advertising, provides you with an opening screen offering 14 general categories. You can refine your search by "drilling down" through the layers of increasingly specialized lists, or you can enter a keyword and Yahoo will conduct a search to try to match it.

If you have something specific in mind, you'll probably get to the information faster with an index tool, which looks through the con-

tent of Web documents as well as their titles. I've found that of the several index tools available, Lycos, also in transition from academic experiment to commercial product, most often comes up with the most useful results. Another good



choice is InfoSeek. Unlike the other tools, InfoSeek charges for its services—20¢ per transaction, less for heavy users. But it includes access to proprietary data, including news from the Associated Press and company profiles from *Hoover's Hand-*

### Web Navigators

#### BY KEYWORD

##### LYCOS

<http://www.lycos.com>

##### WEBCRAWLER

<http://webcrawler.com>

##### INFOSEEK

<http://www.infoseek.com>

#### BY TOPIC

##### YAHOO

<http://www.yahoo.com>

book of *American Business*.

Both Lycos and InfoSeek have a search syntax that takes a bit of effort to learn, even with their help notes. For example, on either system, the search command *president bush -clinton* would find documents containing the words *president* and *bush* but not *clinton* (because of the minus sign). A third search tool, WebCrawler, is easier to use but much more limited. While Lycos and InfoSeek give you an abstract of each document found, WebCrawler often offers only the document's title, which generally isn't very enlightening.

**LOOK AGAIN.** You may want to do multiple searches, because each tool gleans its own data from the anarchic Web—data that are unlikely to overlap what other tools find. I recently wanted information on federal restrictions on the export of encryption software. A search for *cryptology* on both Lycos and InfoSeek turned up useful lists of documents. But only two showed up on both lists of the 10 most promising items as ranked by the services, based on the number of times the word is used and other measures. And the same search on Yahoo turned up a list that shared little with the other two.

Once you have found a site or document that comes close to your goal, you can usually find related material by following the highlighted entries that take you to other Web pages when you click on them. And if you've come across something you think you'll want to return to, make sure to add it to the "bookmarks" or "favorites" list on your Web browser. It can take a fair amount of work to find that elusive site, and you don't want to go through that again.

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Pentium-powered laptops becoming much more affordable. The Latitude XPi series from Dell Computer (800-664-9649) is a good example. Base prices range from \$2,999 for a 75-megahertz



unit with a 10.4-inch passive matrix display to \$4,499 for a 90-Mhz active-matrix version. Standard features for all models, which weigh in at just over six pounds, include 8 megabytes of memory, 4 MB hard drives, and lithium ion batteries. While lacking multimedia features such as CD-ROM drives, the bright displays and good keyboards help make the Latitude XPi a joy to travel with.

### INTERNET

#### APPLE NEWTON ACCESS

A new version of PocketCall communications software offers Internet connectivity to Apple Newton users. PocketCall 2.0 from Ex Machina Inc. (800-238-4738) lets the Newton connect with many mainframe systems and even to the World Wide Web, using text-only Lynx browser. PocketCall includes the software needed to establish an Internet account with Netcom Online Communication Service. PocketCall 2.0 retails for \$119; a free upgrade is available to owners of version 1.

QUESTIONS? COMMENTS? [tech&you@businessweek.com](mailto:tech&you@businessweek.com) on Internet or fax (202) 383-2125



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## QUOTAS: A BAD IDEA WHOSE TIME HAS GONE



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**R**ace and gender quotas, long a festering sore, have become a hot political issue. Republican Presidential contenders Bob Dole and Phil Gramm have promised their abolition. The California Civil Rights Initiative, designed to abolish that state's quotas, seems destined for the November, 1996, ballot. On July 20, the Regents of the University of California voted to end race-based employment and admissions policies, and California Governor Pete Wilson, another Presidential contender, has filed a lawsuit challenging the constitutionality of his state's quota policies.

A July, 1995, Gallup Poll shows that the public is fed up with quotas. Americans reject employment quotas by a margin of 63% to 35% and college-admission quotas by 57% to 39%. Favoring a less qualified "protected minority" over a white applicant is rejected by 84% of the population. Even blacks disapprove of this policy, with 68% opposed and only 22% in favor.

Quotas have many disturbing aspects, so it is not surprising that the public rejects them. Preferences are inconsistent with our color-blind Constitution, and they are strictly illegal under the 1964 Civil Rights Act, which is redundant with prohibitions against quotas.

Quotas are the work of Equal Employment Opportunity Commission interpretive regulations—themselves illegal under the Civil Rights Act—as well as federal judiciary decisions. These decisions, which at the time appeared to be limited rulings to open opportunities for minorities, had far larger implications.

**BIG PICTURE.** For example, in the late 1960s, EEOC compliance officer Alfred W. Blumrosen set aside the statutory focus on intentional discriminatory acts against individuals and redefined discrimination in terms of statistical underrepresentation of groups in the workforce. Under this approach, employers faced discrimination liability if they did not hire minorities in proportion to their percentage of the surrounding population.

This deviation from the Civil Rights Act reached the Supreme Court in 1971 in the case of *Griggs v. Duke Power*. Chief Justice Warren Burger saw the case in terms of opportunity blocked by "credentialism." In its decision, the Court deferred to the EEOC as the implementing agency and accepted what came to be known as the "disparate impact" standard, which defines as discriminatory any

policy or job requirement that does not produce race and gender proportionality.

The disparate-impact ruling made quotas mandatory in order to avoid discrimination lawsuits, though this was not realized at the time. It was not until 1979, in *United Steelworkers of America v. Weber*, which upheld racial quotas, that Burger confronted the quota implications of his *Griggs* opinion. Alarmed, the Chief Justice dissented from the *Weber* decision, accusing the majority of Orwellian reasoning that ignored "statutory language, uncontradicted legislative history, and uniform precedent."

**CASTE SOCIETY?** Neither the court nor legal commentators realized at the time that *Griggs* destroyed equality before the law. However, once racial imbalance became proof of discrimination, white males adversely affected by quotas were deprived of the protection against reverse discrimination that the Civil Rights Act provided. It is impossible to have a civil rights policy that requires remedies for racial imbalance and simultaneously recognize the adverse impact of the remedy on white males.

Over the past two decades, we have inadvertently created a caste society in which there are two classes of citizens: those who are protected by civil-rights laws and white males, who are not. Equal standing under the law is giving way to a status-based legal system akin to feudalism, in which legal rights depend on race and gender.

The emerging status-based legal system has dire implications for the market allocation of resources. Quotas have already emerged in the mortgage market (see this column Jan. 24, 1994, Oct. 3, 1994, May 22, 1995), and some federal-employment policies explicitly prohibit hiring on the basis of merit. Catherine Crier reported on ABC-TV's *20/20* (Nov. 18, 1994) that job postings for U.S. Forest Service fire-fighting positions specified that "only unqualified applicants will be considered," and the Federal Aviation Administration, the agency in charge of air-traffic safety, has recently provided its supervisors with guidelines that state: "The merit promotion process...need not be utilized if it will not promote your diversity goals."

The exclusion of merit is an ironic outcome of a movement whose goal was inclusion. It bodes ill for the U.S. as a competitor in the emerging era of global capitalism.

Paul Craig Roberts is John M. Olin Fellow of the Institute for Political Economy and Distinguished Fellow of Cato Institute in Washington, D.C. He is co-author of *The New Color Line: How Quotas and Privilege Destroy Democracy* (Regnery Publishing, October, 1995).



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BY GENE KORETZ

## THE EQUALIZER: PRODUCTIVITY

It keeps U. S. workers competitive

Perhaps the most forceful argument made by critics of free trade is that it confers an unfair competitive advantage on countries with low wages and lax regulations—permitting them to undermine wages and job growth in the U.S. and other industrial nations. How, for example, can U.S. workers compete with Thais or Malaysians making a fraction as much money?

The answer, claims economist Stephen Golub of Swarthmore College in a recent issue of the Federal Reserve Bank of San Francisco's *Weekly Letter*, is to be found in the dynamic behavior of markets. Low wages in foreign countries usually go hand in hand with low productivity, so that labor costs per unit of output are closer to U.S. levels. And tightening labor markets and productivity gains in developing nations tend

real wages fostered by productivity gains closed the gap. Economic theory suggests that this process will continue.

The other part of the story, says Golub, is that productivity gaps between countries also differ from industry to industry. Thus, while Thailand's wages and productivity in overall manufacturing were about 15% of the U.S. level in 1990, its relative productivity is likely to be greater than 15% in simple products such as textiles but less than 15% in sophisticated products such as machinery. So its comparative advantage will lead it to export textiles and import machinery.

Such dynamics and Golub's analysis of recent trends in the Pacific Basin indicate, he says, "that fears about unfair competition from low-wage developing nations are greatly exaggerated."

## NO LETUP IN U.S. LAYOFFS

Especially for white-collar posts

With the pending merger of Chemical Bank and Chase Manhattan Corp. expected to cost 12,000 employees their jobs, it's clear that America's downsizing trend is still in high gear. Indeed, for managerial and professional workers, the pain has been growing. According to a new Labor Dept. report, these occupations accounted for 24% of all permanent layoffs during 1991-93, compared with just 13% in 1981-83.

What's more, while it was mainly low-paid managers and professionals who got axed in the early 1980s, staff cuts in the 1990s are affecting employees across the income spectrum. These days, sums up the Labor Dept. report, "even for managers and professionals, being at the top of the earnings ladder appears to provide less protection when budgets become leaner."

## A WHOOSH FROM WINDOWS 95?

Brisk sales may boost the economy

If the economy picks up steam during the rest of the year, Microsoft Corp. Chairman William H. Gates III will deserve a modicum of credit, says economist Charles Lieberman of Chemical Securities Inc. That's because hundreds of thousands of computer owners will be switching over to Windows 95.

Industry reports indicate that U.S. and Canadian consumers snapped up some \$90 million worth of Win95 in the first four days. And that includes not only the sales of updated software products and computers with Win95 already installed nor the big bucks that computer users will spend for hard disks and memory to bring their hardware up to date.

Add it all up, and there's a good chance that computer-related sales will hype August's final nonauto retail sales by at least 0.3%, says Lieberman. And with school starting and Christmas a few short months away, the boom is only beginning.

## DISCOUNT DUDS: A MIXED BLESSING

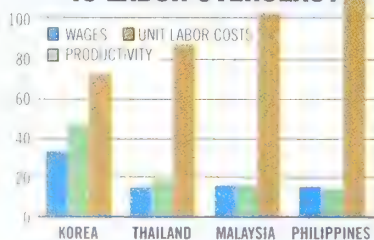
They fight inflation but hurt stores

Among items whose price behavior have helped keep inflation at bay in recent years, apparel is clearly a standout. America's clothing prices have been trending down steadily since the start of last year (chart).

Margaret M. Cannella of Citicorp says changes in consumer demographics and clothing retailing are sparking a slump. For one thing, a drop in the number of women entering the workforce has pounded specialty apparel shops, which catered to their needs for high-priced wardrobes. After rising nearly 11% from 1985 to 1990, the number of employed women between the ages of 25 and 34 has fallen by some 3.6% over the past five years.

At the same time, giant discount and department store chains have been aggressively expanding their apparel departments, gobbling up an increasing share of clothing sales at the expense of smaller retailers and specialty shops. The upshot has been rising supply in the face of slowing demand, growth and the eruption of heavy price discounting and promotional efforts to bring inventories in line with demand. Many U.S. retailers are also merging and closing stores. All of which suggests that apparel prices will remain subdued for some time to come.

### JUST HOW CHEAP IS LABOR OVERSEAS?



▲ PERCENT OF U.S. LEVEL\*

\*MANUFACTURING INDUSTRIES, 1990 DATA

DATA: STEPHEN GOLUB, SWARTHMORE COLLEGE

to drive up wages and spark currency appreciation.

The chart above tells the tale. Although 1990 factory wages and other compensation in these four developing countries amounted to only 14% to 32% of U.S. pay, unit labor costs were 71% of U.S. levels in South Korea, 86% in Thailand, and actually above U.S. levels in Malaysia and the Philippines. Low productivity in these countries, compared with the U.S., considerably narrowed any competitive advantage conferred by low wages.

Interestingly enough, back in 1970, unit labor costs in these four countries were less than half U.S. levels. In the intervening 20 years, a combination of currency appreciation and increases in

### CLOTHING PRICES KEEP PLUNGING



▲ PERCENT CHANGE OVER 12 MONTHS

DATA: LABOR DEPT.



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# STEADFAST SHOPPERS KEEP THE EXPANSION ROLLING

## U.S. ECONOMY

That constant beat you hear is the footsteps of consumers marching to the latest sale or to their real estate agent's office. Even in the first half, when the economy looked feeble, consumers were right there—wallets open, ready to help businesses pare down inventories and stave off recession. And from all the signs, households will remain steadfast in the second half.

For one thing, job jitters, so prevalent earlier in the expansion, have diminished. Income growth, while robust because of slower job growth, remains supportive. Credit is flowing generously through the banking system. All this is giving consumers a good feeling about the coming months—enough so that more of them this summer are shelling out big bucks for new houses (charts).

### HOUSEHOLDS STILL FEEL UPEAT



DATA: CONFERENCE BOARD

Consumer spending last quarter was even stronger than first thought, resulting in an upward revision to economic growth. Real gross domestic product rose at an annual rate of 1.1% in the second quarter, according to the Commerce Dept.'s latest numbers, up from the originally reported advance of 0.5%.

As it turns out, consumer lays rose a sturdy 3.4% instead of 2.5%. Consequently, overall demand by consumers, businesses, and government increased 2.5%, higher than the 2.1% gain reported earlier.

A healthy pace of consumer spending is helping businesses to trim their top-heavy inventories. Excluding the farm sector, business stockpiles rose a bit less in the second quarter than first estimated—up \$31.9 billion instead of \$32.9 billion—but that was far below the first quarter's \$49.1 billion advance.

Although that slower growth was a big drag on the economy last quarter, leaner stockpiles and continued spending are laying the groundwork for better economic growth in the second half.

### IT DON'T LOOK FOR

a return to last year's brawny performance. Consumers are in good shape—but not at good. First of all, the economy is not creating as many jobs this year as in 1994. Second, the cyclical surge in housing and durable goods last year exhausted a lot of spending power and pumped up debt loads.

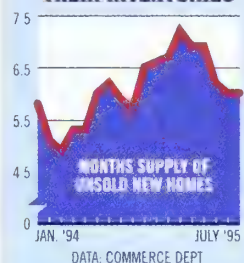
Also, the 1996 federal budget will be a drag on the economy. Moreover, the Federal Reserve's rate hikes, which ended in February, are still squeezing activity.

Even the Fed thinks so. The minutes of its July 5-6 policy meeting, released only recently, show that nearly all members viewed policy as "somewhat restrictive." Only one of the 12 members of the policy committee voted against the July 6 quarter-point cut in interest rates. Given that breadth of sentiment and given that the economy seems most likely to continue along a modest growth path, chances for another small cut at the Sept. 26 meeting remain alive.

The Fed's willingness to cut interest rates a bit may have played a part in keeping consumers feeling upbeat. Consumer confidence, although down a shade in August, held at a fairly high level. The Conference Board's index dipped to 101, down from 101.4 in July. Historically, a level around 100 is a strong reading.

Households are feeling better about the future. Although they gave a more downbeat assessment of present conditions, they rated prospects six months from now much higher than they did in July. This expectations component of the overall confidence index is more closely correlated with spending patterns.

### BUILDERS CLEAR OUT THEIR INVENTORIES



DATA: COMMERCE DEPT

**FAITH IN THE FUTURE**, especially when combined with this summer's lower mortgage rates, is a key reason why home buying has been so strong. Sales of existing houses jumped 5% in July, to an annual rate of 3.99 million. That was the third consecutive increase and the highest level in more than a year.

Sales of new houses are also up for the third month in a row. From an annual rate of 712,000 in June, they edged up to 715,000 in July, also the highest in more than a year. Since hitting a three-year low of 575,000 in February, sales have grown the strongest in the West and South. The gain in the Midwest has been more modest, and homebuying in the Northeast is actually down some 20%.

It's very likely that this year's surge in homebuying is about to top out, however. That's because the gains in recent months reflect declines in mortgage rates earlier in the year. By mid-July, the average rate on a 30-year fixed-rate mortgage had fallen to 7.41%, according



to the Federal Home Loan Mortgage Corp. Since then, rates have risen to 7.88% by late August.

That level of rates is still consistent with a healthy pace of sales, but unless rates start falling again, there is nothing to spur further gains. Indeed, mortgage applications to buy a house had surged 44% from early January to early June, but since then they have dropped 14% by mid-August. That pattern suggests that housing demand is now falling off and that home-sales data this fall will look weaker.

Still, sales of new houses this summer have been sturdy enough to generate new building activity that should continue into the fall. Builders' supply of unsold new homes had reached a 7.2-month supply, relative to the pace of sales, but the July inventory stands at a more comfortable 6 months.

**WHEN HOUSING DEMAND** is at a high level, it bodes well for sales of home-related durable goods. And sales of such big-ticket items as furniture and appliances have indeed strengthened this summer, helping stores to wrestle their inventories into better shape.

In the process, though, hard-goods manufacturers have taken a hit. Orders taken at durable-goods factories fell 1.7% in July, and since reaching their recent peak in January, they are down nearly 5%.

But the weakness in orders has been concentrated in the transportation sector, especially the auto industry.

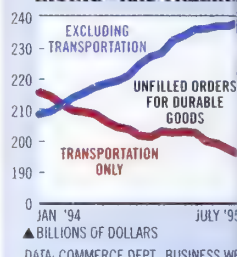
Excluding bookings in transportation, orders are 1.3% below their January level. Rising orders for electronic equipment, reflecting strong capital spending in that area, have helped to buoy the total.

Moreover, excluding the transportation sector, filled orders are growing (chart). That means in durable-goods industries have plenty of work in pipeline, and once Detroit's production picks up again as it is slated to do in coming months, the overall factory sector will show more bounce.

Detroit accounted for much of the weakness in July durable-goods orders. But that largely reflected inadequate seasonal adjustment for the plant shutdowns during the month. For that reason, August orders are likely to look stronger. August car sales also appear to be bouncing back from their weak July showing, also reflecting seasonal quirks.

Thanks to consumers' relentless support, the economy's inventory adjustment is running its course quickly and will probably be complete by the end of the third quarter. After that, as long as households keep beating a steady rhythm, the expansion should keep marching well into 1996.

## WHERE THE BACKLOG RISING—AND FALLING



## AUSTRALIA

# PEPPY GROWTH MAY BRING A TUG ON THE REINS

Unlike policymakers of most other industrialized nations, Australia's central bank is in a restrictive mode. But the reason is not hard to figure: The Reserve Bank of Australia is trying to fight inflation and a weak currency as the outlook calls for continued healthy growth.

The Aussie economy grew at a quarterly rate of 1% in the second quarter, up from a 0.3% gain in the first. Real gross domestic product was up 3.7% from a year ago, near the top of the 3%-to-4% range thought by the RBA to be sustainable, noninflationary growth. A surge in inventories led the gain.

The third quarter got off to a good start as well. Retail sales

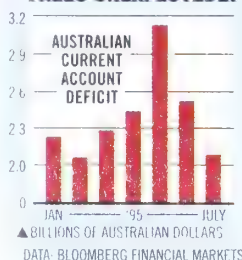
rose 1.1% in July, and the current-account deficit took a surprise fall. The July trade gap narrowed to A\$2.09 billion (U.S. \$1.52 billion), down from A\$2.52 billion in June (chart). Goods exports rose 8.8% to a record high. With the chronic deficit improving, the Australian dollar continued its two-month climb, rising on Aug. 29 above U.S. 75¢ for the first time in seven months. The dollar had lost 6.4% of its value in the first half.

The RBA's problem is that inflation is also rising. The nonfarm GDP deflator rose 2.1% in the year ended in the second quarter, up from a 1.4% pace in the first. And consumer prices rose 4.5% in the

12 months ended in June, the fastest rate in more than four years. Higher inflation, plus worries that the Aussie dollar cannot sustain its recent rally, may soon prompt the central bank to raise the overnight cash rate for the first time this year, on top of three hikes in 1994.

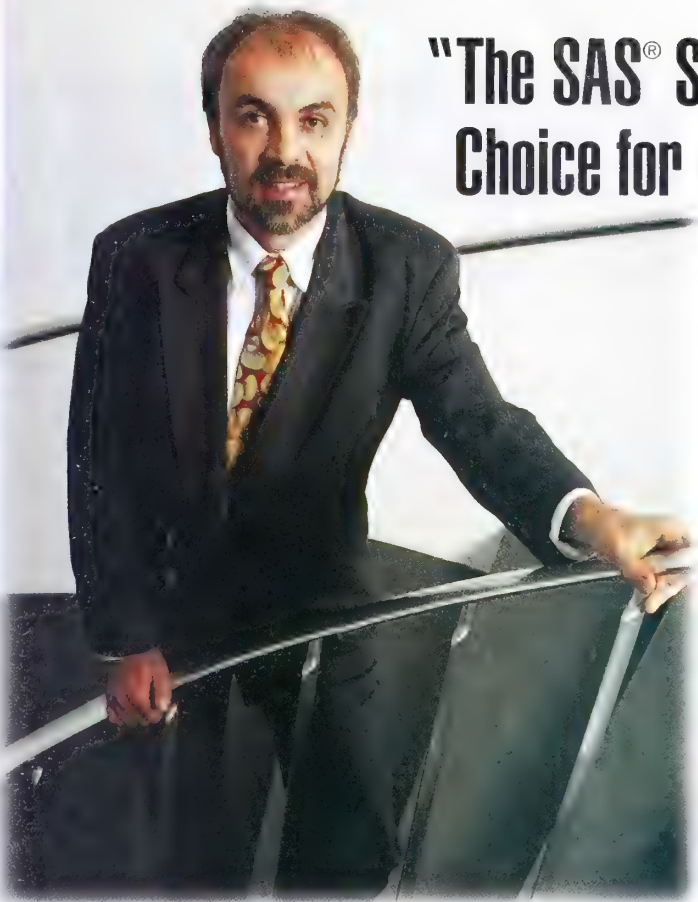
One optimistic sign for the inflation outlook is the recent pact between the unions and government, which will limit yearly pay raises to 2%—well below the current inflation rate. The resulting drag on incomes, however, means that consumer spending will weaken in coming quarters. Still, the RBA emphasized inflation trends rather than growth in its Annual Report, released on Aug. 23. That's just one more reason why analysts are betting on another rate hike.

## THE TRADE GAP FALLS UNEXPECTEDLY



The RBA's problem is that inflation is also rising. The nonfarm GDP deflator rose 2.1% in the year ended in the second quarter, up from a 1.4% pace in the first. And consumer prices rose 4.5% in the

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They're finding answers in the SAS System, which enables over 70 financial analysts to advise portfolio managers on the best portfolio mix. "Our strategy is to find ways to enable analysts and financial advisors to handle information more easily and quickly," says UBS Vice President Beat Moser. "What that meant was finding a software tool that could eliminate the redundancy of information and time caused by the use of several different analysis products—each limited in terms of functionality and ability to access key data. And it meant finding a tool that allowed applications to be developed, and changed, fast."

**Smart Move, Smart Money** Moser believes that UBS has resolved those challenges in their choice of the SAS System as their strategic software. "Our previous system required many labor-intensive steps as data was moved from one software product to another," recalls Moser. "Today data access, management, and summarization is handled automatically by the SAS System. This has given us productivity gains of up to 200% in some areas. The SAS System is fully integrated and meets most of our analysis needs—it's our strategic choice in various research units of our bank."

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## COVER STORY

# LAND OF THE

**B**link, and another billion-dollar company may have disappeared. Step out for coffee, and an entire industry could be transformed.

Almost without warning, the U.S. has entered a new era of bigness. Since the beginning of 1995, more than \$270 billion worth of mergers and takeovers have been announced, according to Securities Data Co. And that could mark the start of a merger wave that may dwarf the merger mania of the 1980s. Chase-Chemical, Disney-ABC, Time Warner-Turner—these are just the tip of an economywide move toward combination and consolidation (table).

Today's deals are not the financially driven hostile takeovers and leveraged buyouts that dominated the 1980s. No

raiders are carrying out bags of cash this time around. Now, it's the corporate leaders of America who are riding the merger boom. Their goal: to acquire the size and resources to compete at home and abroad, to invest in new technology and new products, to control distribution channels and guarantee access to markets. "We are moving toward a period of the megacorporate state in which there will be a few global firms within particular economic sectors," says Steven Nagourney, chief investment strategist for Lehman Brothers Inc.'s private client group.

That's certainly true in the media industry, where the race to lock up key distribution channels such as television and cable networks just got more frenzied (page 40). Market dominance is also driving such mergers in the drug industry as Merck & Co.'s purchase of Medco

Containment Services Inc. "As your competitors get big, you're almost forced to get bigger to stay equal," says Norman C. Selby, head of McKinsey & Co.'s pharmaceutical practice. "It's a continual game of catch-up."

**TRAILING TITANS.** Other deals are driven by a need to build up as U.S. companies take on global competitors. The Chemical-Chase merger produces a bank that's No. 1 in U.S. but only 21st in the world, by assets. And the combination of Upjohn Co. and Sweden's Pharmacia, announced on Aug. 20, will create a titan that only ranks about ninth in sales among drugmakers worldwide.

Besides adding sheer size, acquisitions can provide an instant presence in foreign markets. Scott Paper Co. was a

quired by Kimberly Clark Corp., in large part, because Scott had strengths in Europe that Kimberly lacked. And Philadelphia-based Crown Cork & Seal Inc. recently said it would buy France's CarnaudMetalbox to create a global packaging giant.

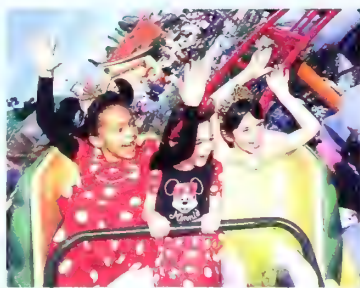
Many of these mergers would not have been possible without today's permissive climate in Washington. With a Republican Congress and with the Clinton Administration on the defensive, companies no longer fear the knock on the door from the antitrust police. While noting that some transactions are "troublesome," Federal Trade Commission Chairman Robert Pitofsky observes that "many of these mergers are not between competitors and represent a healthy restructuring of certain industries, especially those with vast overcapacity."

## Bigger, Bigger, Bigger...

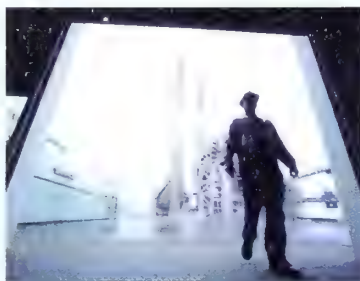
**ENTERTAINMENT** ▶ Just about everyone is trying to dominate this hot U.S. export. Reason: Vertical integration is supposed to yield clout in the Information Age. Result: Disney, Seagram, and Westinghouse are all doing huge deals. Now, Time Warner is wooing Turner Broadcasting.



**UTILITIES** ▶ Slow growth in domestic power consumption and increased competition from deregulation have spurred deal mania in the staid electric utilities industry. PECO Energy bids \$3.8 billion for neighbor PP&L Resources; Union Electric and Cipsco merge for \$1.2 billion.



◀ **FINANCIAL SERVICES** The goal here is to squeeze out costs and earn economies of scale. That's a big reason behind Chemical's \$10 billion merger with Chase and First Union's \$5.4 billion acquisition of First Fidelity Bancorp. Now, can these behemoths increase sales?





# GIANTS

## Today's merger wave is different from '80s mania. The overriding goal: Market dominance

Companies are taking advantage of deregulation to make larger combinations. New rules lifting barriers on state banking set to take effect in September, for example, will ignite a new round of cross-country mergers. The proposed elimination of the Interstate Commerce Commission, which reviews railroad mergers, may spark combinations among rail carriers. One possibility: a Norfolk Southern Corp. takeover of Conrail Inc. The passage of the telecom deregulation bill, expected next year or next, may be the signal for some of the best mergers of all time, especially if the old Bell system starts reassembling itself. "It's not unreasonable to see [regional Bell operating companies] merging over

the next several years," says Daniel Reidenbach, vice-president of Merrill Lynch & Co. The most likely candidates: Bell Atlantic Corp. and Nynex Corp., which already jointly run a cellular service.

The drive to bigness indicates CEOs such as Chairman Louis V. Gerstner Jr., who announced a plan to split Xerox into smaller companies when he took over the industry in April, 1993. "The industry's coming our way," Gerstner told Wall Street analysts on July 31. Indeed, the trend is for corporate customers to start to deal with fewer—and therefore bigger—suppliers.

Inevitably, some of the mightiest players will be trampled in the race for market dominance. Apple Computer Inc., with only about a 10% share of the personal-computer market, may find that software developers will concentrate

their efforts on the much larger Windows market—which could badly damage Apple sales. Apple CEO Michael H. Spindler is pushing to boost Apple's market share—but his efforts may be too late in the face of the Windows 95 juggernaut. Rumors have circulated—denied by Spindler—that Apple could wind up being acquired by IBM, Canon, Oracle Systems, or Sony.

**TEMPTED.** Is this new wave of mergers good for the U.S. economy? There's reason to be skeptical. The inevitable result of these mergers will be a new round of downsizings and layoffs, as companies attempt to find cost savings. Moreover, the megacompanies may be tempted to take advantage of their new-found market strength by raising prices.

But it may be that what used to be big is merely midsize when measured on a global stage. "I would be very uncomfortable in a world of 200 companies," says Lawrence J. White, an economist at New York University. "We are not anywhere close to that." Indeed, he notes, over the past 15 years the U.S.'s largest companies have accounted for an ever smaller share of economic activity.

Perhaps the larger danger is that many of the benefits of size will prove to be illusory. While managers struggle to absorb their new acquisitions, they may be vulnerable to nimble entrepreneurs. For now, though, the big rule.

*By Michael J. Mandel with Christopher Farrell in New York, Catherine Yang in Washington, and bureau reports*

... Acquisitions totaled more than \$270 billion so far this year—a record pace. Here are some industries being swept by deal mania.



**CONSUMER GOODS** ▶ Deals are largely driven by a need to compete globally and a fight for shelf space. Examples: Kimberly-Clark becomes world's largest tissue maker by paying nearly \$7 billion for Scott Paper; raider Bennett LeBow is trying to buy 15% of RJR Nabisco.



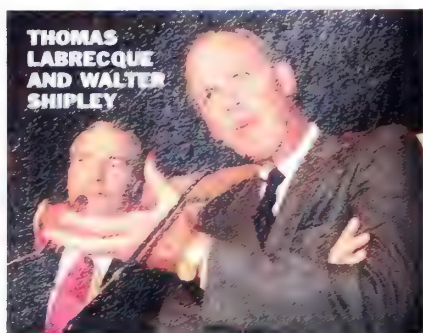
◀ **HEALTH CARE** Drugmakers, managed-care networks, hospitals—everyone in health care seems to be merging. One example: Upjohn is hooking up with Sweden's Pharmacia in a \$6 billion merger. Cost-cutting aside, hefty deals let suppliers negotiate deals with large purchasers.



◀ **TRANSPORTATION** Deregulation has rocked every sector. Among railroads, Union Pacific is paying \$5.4 billion for Southern Pacific; Burlington Northern anted up \$4 billion for Santa Fe Pacific. Savings come from sharing overhead and cutting duplicative routes.



## COVER STORY



THOMAS  
LABRECQUE  
AND WALTER  
SHIPLEY

# WOW! THAT'S SOME BANK

Chase and Chemical: Will clout rule?

**F**or eight years, Walter V. Shipley has taken a week each summer to golf in Scotland or Ireland with Robert E. Allen, CEO of AT&T, and their wives. This year, though, Scotland's verdant links weren't so relaxing. "I'd end up sometimes playing 36 holes of golf, go have a drink, have dinner, play gin rummy, and then get back on the phone" to New York, he says.

Shipley certainly appeared relaxed enough: He shot an 82 at St. Andrew's, his best round there ever. To throw off rumormongers, Shipley stuck to his entire regular vacation schedule, even going on a late August fishing expedition in Canada. All the while, Allen had no idea that his good friend was embroiled in negotiations with Chase Manhattan Corp.'s Thomas G. Labrecque to create the nation's largest bank.

On Aug. 28, Allen got the news. So did the banking world: Shipley would join his Chemical Banking Corp. to venerable Chase, the bank of the Rockefellers. At \$297 billion in assets, the new Chase—the bank will keep the older name, even though Chemical clearly will dominate—will dwarf even Citicorp, long the largest U.S. bank. It will have \$20 billion in equity to invest where it pleases, a sum exceeded by only three other banks in the world. "Chase will be able to compete in a manner to which few institutions can aspire," Shipley exults.

**TOP PLAYER.** The numbers are breathtaking. True, the combination would rank just 21st in assets worldwide, behind a host of giant Japanese and European competitors. Yet with more than \$163 billion in overall deposits and some 4 million consumer accounts, Chase will be the dominant retail bank in New York. Its \$20 billion portfolio of credit-card balances will be fourth in the nation. It will be the global leader in emerging-markets underwriting and trading revenues. And with \$19 billion



**Banking's New Powerhouse**

*How the combination of Chase Manhattan and Chemical rank in its key markets*



an syndications under its belt so this year, according to Loan Price Corp.'s *Gold Sheets*, the new Chase be far and away the leader in that ring business, giving it entrée into active and multifaceted customer relationships around the world (table). y combining two operations that pete directly in many markets, over, the new Chase expects to cut 10 employees and \$1.5 billion in an- expenses by the first quarter of . But that's the easy part. The big- question: Can Shipley engineer last- revenue gains from a combination recedented in its size and diversity, lucing an organization that yields it growth long after the excess costs

have been wrung out? "They can get costs down in two years," says John B. McCoy, chairman and CEO of Columbus (Ohio)-based Banc One Corp. and a veteran of more than 100 acquisitions. But "can they get the revenue side pumped up with the right focus?"

The early evidence doesn't point to an easy home run. Shipley and Labrecque both have produced only mediocre long-term results at their institutions and enter into their marriage with some likely cultural barriers and no articulated vision beyond the need to cut costs. The banks' retail operations face a market in revolution, where success increasingly depends less on size than on nimbleness and creativity. Their electron-

ic home-banking effort lags. And their mutual-fund products, though they have performed well, have relatively skimpy sales compared with those of rivals.

More to the point, the banking industry is consolidating around them at a breakneck pace. Well focused rivals, including J.P. Morgan & Co., Banc One, and nonbanks such as Charles Schwab, have formidable expertise in many of the new Chase's businesses. As he leads Chase into the 21st century, Shipley must walk a fine line between maintaining the heft that generates market clout and avoiding bulk that translates into inefficiency, undue risks, and a diffusion of corporate energy.

As CEO of Chemical, Shipley vowed

## WORLDWIDE WHOLESALE BANKING

### #1 GLOBAL LOAN SYNDICATION

Chemical led this booming market before the merger, doing \$160 billion in 1995 deals; Chase is strong in complementary industries

### #1 TRADING

Chemical's focus is on market making; Chase has emphasized customer transactions in growth areas such as emerging markets

### #1 GLOBAL CUSTODY

Chase leads in recordkeeping and processing of corporate customers' securities worldwide

### WEAK SPOT: UNDERWRITING

Although both banks are picking up steam, neither broke into the top 10 debt underwriters for 1994

## U.S. CONSUMER PRODUCTS

### #1 MORTGAGE LOAN SERVICING

The combined banks have a massive \$125 billion servicing portfolio, thanks in part to acquisitions since 1993

### #3 MORTGAGE ORIGINATION

Both banks are major players; combined, they will have \$20 billion in originations

### #4 CREDIT CARDS

Chase had lost ground but is regaining share; Chemical has many lucrative co-branding deals

### WEAK SPOT: MUTUAL FUNDS

Despite strong performance of its Vista funds, Chase has lagged behind most brokers and mutual-fund companies in assets

## NEW YORK RETAIL BANKING

### #1 CONSUMER DEPOSITS

With \$32 billion in deposits, the new Chase will have more of the New York retail market than any rival

### #1 BRANCH BANKING

Ditto—a combined 480 branches in the New York area far outpaces competitors

### #1 MIDDLE-MARKET LENDING

Chemical has long dominated in New York and Long Island; Chase is stronger elsewhere in the region

### WEAK SPOT: ELECTRONIC BANKING

Citibank and others are ahead





that the bank would be a leader in its chosen markets. But in practice, his bank has a portfolio of a dozen or so businesses—not all of which produced top-tier results. Now, as CEO-designate of the new Chase, Shipley lauds the synergies in the deal and sets lofty financial goals: He says the bank aims to get costs down close to 50% of revenues, low for a bank, and generate a return on equity of 18% or higher. But all Shipley says about long-term goals is that Chase will “plow forward as one of the world’s great global banks.”

He and Labrecque say the bank has some two dozen key businesses, and they plan to make substantial investments in half a dozen of them to give Chase leadership positions.

**HUGE THREAT.** Shipley exudes confidence about the new Chase. But many banks have suffered when they have tried too hard to diversify broadly—one reason big money-center bank stocks long underperformed those of their regional brethren. Citicorp, most notably, learned its lesson all too well in the 1980s: After a disastrous immersion in commercial real estate that even, temporarily, put Citi on a short leash with its regulators, the bank vowed to change its ways and manage for profitability rather than scale. “In the past, we tended to run the company to occupy space,” Chairman and CEO John S. Reed told analysts in February. He vowed that henceforth, “we’re going to run the company for performance” and not try to be in every market.

Without question, Chase’s doubling will present a formidable competitive threat to many of its wholesale banking competitors. A top London foreign exchange specialist says that a merged Chase “will certainly be a stronger force.” It will be tough to beat in the custody business, too. Bank of New York, for example, has been actively snapping up custody operations in a bid to build scale. But, says one bank analyst, “combine [Chase and Chemical’s trust and custody operations], and can you picture what that does to Bank of New York? It blows them away.” A Bank of New York spokesman says the company “has increasingly become a player in global custody [a segment of the custody business]. This merger does not change that.”

In retail banking, though, size is only a starting point. Experts such as Frank Woosley, director of the financial institutions consulting practice at Deloitte & Touche, predicts that 450,000 jobs will

disappear from the business in the next decade as banks go electronic. “The only thing that matters about having a big customer base is if you segment it and do a good job with each segment,” he says. Adds Tom D. Seip, head of retail brokerage for Charles Schwab & Co.: “Size will make them a tougher competitor. But just better distribution won’t make or break them. They have to administer the level and type of services that customers want.”

## Shipley praises the synergies, but all he says a

The new Chase would lag behind Citi and others in electronic banking offerings, an area both Shipley and Labrecque admit they need to steer more investment toward. As nontraditional competitors enter the retail fray, Chase could become even more vulnerable. “One of the great dangers of this merger is that they are going to be tremendously inwardly focused for the next three years,” says David M. Partridge, director of the financial institutions

practice at Towers Perrin. “For Fidelity, Schwab, and Citicorp, this is a wonderful opportunity to take business away from the combined bank.” Mutual funds and credit cards might be especially vulnerable.

All told, “I’d have to concede the most attractive part [of the deal] is economies they’re talking about,” says John Neff, senior vice-president managing partner of Boston-based Wilmington Management Co. and a holder

of 2.6 million shares of Chemical stock. Certainly, those savings will be substantial. Chemical’s widely praised 1991 merger with Manufacturers Hanover Co. ultimately excised 6,200 jobs and \$100 million in annual costs.

But integrating the branch systems of Chemical and Manny Hanny took close to two years. A major hurdle was accommodating the gradual melding of the two corporate cultures. With the new Chase, too, there is the poten-

## THE NEXT FEEDING FRENZY WILL FEATURE SMALLER FISH

**W**ho’s next? The eye-popping \$10 billion alliance of Chemical Bank and Chase Manhattan has sent a message to bankers everywhere: If such titans are fodder for the industry’s consolidation frenzy, just about everyone is vulnerable. So if they haven’t already been checking out their neighbors—fearfully or covetously—bankers all across the country are now eyeing one another anew.

Yet despite the New Yorkers’ megalliance, odds are that the most intriguing deals going forward won’t be among the biggies. The eight or so U.S. banks with more than \$100 billion in assets probably will stand pat for a while and exploit their global lending businesses. Once Chemical and Chase slim down, bank-watchers say, there won’t be much fat left to cut in this segment.

**“SUPERREGIONALS.”** Instead, banking’s merger frenzy will likely be most fierce in the middle ranks. There, a few dozen outfits with \$10 billion to \$100 billion in assets and turf that spans one or just a few states are finding they can’t go it alone anymore. Revenue growth is too hard to come by in their overbanked

markets. “The whole industry is rife with overcapacity,” says Douglas Pratt, portfolio manager at Invesco Strategic Financial Services Fund in Denver. “If the big guys are doing it, why shouldn’t the little guys do it?”

In fact, many of the 277 mergers

### Movers, Shakers, Merger Makers

**AM SOUTH BANK**

**16.7** Preeminent Alabama bank with attractive holdings in Florida markets

**SIGNET**

**13.1** Virginia bank with a strong mid-Atlantic franchise and strong market-research unit



culture clash. While the two CEOs that the banks' cultures are extraordinarily compatible, others are skeptical. Gerard L. Thomas, chairman and CEO of First Chicago Corp., which is using task forces to implement a merger with Detroit's NDB Bancorp Inc., speaks from experience when he says that merging two corporate cultures "is very hard work."

The trouble spot on the horizon could be the new bank's crowded executive office. Of five top executives, Chemical is supplying three, including, of course, the CEO. Shipley will spend most

of his time on retail banking and national consumer products such as credit cards, while Labrecque will focus on wholesale banking, information services, and risk management. Under the two top officials will be a senior vice-chairman, Chemical's Edward D. Miller, and two vice-chairmen. As if that's not enough complexity, the bank's Labrecque is not the heir apparent, says he suggested leaving the succession question open, but the result-

ing uncertainty could set off a disruptive horse race a few years hence. Then there are possible antitrust problems. With a commanding share in clearly defined local markets such as middle-market lending and branch banking, the new Chase may be forced to divest some of its holdings, according to antitrust attorney and former Justice Dept. Antitrust Div. official Donald J. Baker. He predicts that they are "probably going to sell off some branches—some of which they would have closed anyway," and adds that they may have to sell some foreign offices, too.

the banking group at UBS Securities Inc., is impressed with the merger's potential for savings but also has qualms. "There are risks that are very hard to quantify relative to the control of this bank," he says. Banc One's McCoy, indeed, argues that size can kill if managed improperly: "If you don't know how to drive a race car and it goes 200 miles per hour, you can kill yourself in the first 100 yards," he says.

If Shipley can manage the massive consolidation, the new Chase will have enormous cost savings to propel it forward—\$600 million in the first year of the combined companies, an additional \$450 million in the second, and a final

## Long-term goals is that Chase will "plow forward"

his time on retail banking and national consumer products such as credit cards, while Labrecque will focus on wholesale banking, information services, and risk management. Under the two top officials will be a senior vice-chairman, Chemical's Edward D. Miller, and two vice-chairmen. As if that's not enough complexity, the bank's Labrecque is not the heir apparent, says he suggested leaving the succession question open, but the result-

Shipley must move fast to get this deal together. Too much time dithering, and he risks losing momentum. "This is not the time for them to sit and twiddle their thumbs," says Thomas H. Hanley, head of bank research at CS First Boston Inc. "The hard decisions have to be made immediately and executed immediately."

Yet combining two organizations of such size may create problems no one has foreseen. Gerard L. Smith, head of

\$450 million in the third. Executives at the two banks are clearly excited, as are investors such as Michael F. Price, who shook up Chase when he disclosed a 6.1% stake in the bank in April. Engineering long-term revenue growth for the biggest bank in America will prove a serious challenge. But if the deal works as planned, Shipley's next vacation ought to be a lot more relaxing.

*By Kelley Holland, with John McEehan, in New York, and bureau reports*

so far this year—worth some \$1 billion in all, according to Securities Data—among such middle-market firms. In July, Detroit-based NBD Inc. cut a \$5.3 billion deal with First Chicago Corp., for instance, creating a \$113 billion "superregional" that covers much of the Midwest. A few weeks earlier, North Carolinian First Union Corp. agreed to a \$5.1 billion for New Jersey's Bancorp., creating a \$115 billion Mid-Atlantic powerhouse.

The goals in these deals vary, depending on the size of the deal. Cutting costs by cutting staff and shuttering duplicate branches, for instance, is a big driver for other recent superregional deals as well as for Chase-Chemical. But the New York bankers aren't trying to spread their reach across more states. "The world is their market," says Wharton School Professor Anthony M. Santomero. By contrast, the superregionals still view geography as crucial, so they're trying to spread their

costs over millions of domestic customers, usually in contiguous states.

Of course, expenses do tend to grow. Banks need expensive technology—from home banking to improved automated teller services—to compete. Such costs helped drive Pittsburgh's Integra Financial Corp. into the arms of Cleveland-based National City Corp. in a \$2.1 billion deal announced on Aug. 28.

**ENDANGERED SPECIES?** The latest wave of consolidations almost surely will reshape banking for good. Gerard L. Smith, managing director at UBS Securities Inc., says the trend won't end until the 25 largest banks hold 80% or more of the industry, up from 60% now, and he expects to see the emergence of a truly national bank. The regional bank with assets under \$50 billion may be an endangered species.

For investors, however, banking consolidation is a risky bet. Speculators have bid up stocks sharply, driving the Standard & Poor's major regional bank index of 23 stocks up more than 34% for the year, compared with a 22% rise in the broader Standard & Poor's 500-stock index. That's partly why bankers can afford to pay for their acquisitions with stock instead of cash. But with so much expectation built into stock prices, there could be disappointments down the road.

*By Joseph Weber in Philadelphia and Suzanne Woolley in New York*

*market speculating that more mergers are coming, bank prices are soaring. Here are some likely buyers or targets:*

DATA AS OF 8/29/95

**CoreStates**

 **Meridian**

**4** A leader in check processing and trade services; export-import financing

**15.4** Small Pennsylvania-based bank in a rapidly consolidating region

**UJB FINANCIAL**

**BANC ONE**

**7** One of New Jersey's last midsized independents in a growing market

**14.5** Fast-expanding Ohio superregional on the prowl for acquisitions



## COVER STORY

# TIME WARNER TURNER: NICE SCRIPT, BUT...

Is Levin offering too much to muscle past Disney?

**T**he entertainment biz is nothing if not flexible. Not so long ago, Walt Disney Co. Chairman Michael D. Eisner was pooh-poohing big-ticket acquisitions. Time Warner Inc. Chairman Gerald M. Levin, desperate to pare debt from his balance sheet, wanted out of his 18% stake in Turner Broadcasting System Inc. And Ted Turner was adamant in his refusal to do any deal that left him second fiddle.

The talk sounded good at the time. But now Eisner is paying \$19 billion to buy into Capital Cities/ABC. And in the wake of that megadeal, Levin and Turner are working to fashion another: Levin has offered a dazzling \$8 billion-plus to buy TBS, and Turner is said to be enthusiastic. Their talks are setting the stage for a merger that would catapult Time Warner past Disney to regain its title of world's largest media company.

**PAYING DEARLY.** Make no mistake: This deal, if it comes off, is all about scale. The cash and technology needed to beam movies, TV, and information to the world's billions are demanding that entertainment companies become, simply, bigger. Turner seems willing to subsume his imposing ego to the reality of an industry increasingly dominated by giants. Although he runs several thriving global businesses, one associate says, Turner feared being "closed out of the loop."

Levin, likewise, clearly sees the value of bulk. A deal with TBS would create a media conglomerate of unique depth and breadth in

movie libraries, studios, cable properties, and publishing. Time Warner would gain international reach and expertise, features its cable and movie businesses plainly lack. And it would net Turner's singular talent for turning old copyrights into new revenue opportunities.

That's why Levin appears willing to pay so dearly. By offering the stock equivalent of \$35 a share, he would put up a staggering 17 times TBS's projected 1995 cash flow, well above the 12 times

Disney paid for ABC. Besides diluting Time Warner shares by 50%, the deal would do nothing to reduce the company's \$15 billion debt burden that spooked Wall Street. "This is such a lucrative transaction that, in order for shareholders to win, there has to be a tremendous earnings increase," says a source close to Turner.

**IN THE WINGS.** Clearly, this is no done deal. John C. Malone, whose Tele-Communications Inc. owns 21% of TBS, could block the purchase any time. TCI chairman won't buy into a deal, industry sources say, unless Levin make it worth his while. He already has turned down cash for his stock, fearing the resulting tax bill, and may instead demand a sweetheart price for HBO Inc. and the Turner networks' TCI's cable systems. Even if he were to make such concessions, industry executives

who watched Malone jump ship in Barry Diller's push to acquire Paramount Communications Inc. say Levin can't rely on Malone's support until the ink is dry.

Then there are other potential bidders in the wire. General Electric Co., which has made no secret of its desire to fuse Turner with NBC Inc., could emerge with a fresh bid. And knowledgeable industry executives say Rupert Murdoch's News Corp. or even Disney might make a run for TBS. A Disney source says executives in Mouseland are crunching the numbers.

It's a good time for Turner to find the partner he so needs. His business is going gangbusters and should bring cash flow of \$600 million this year, 50%, figures Merrill Lynch & Co. analyst Jessica R. The CNN news network, the movie channel, and Cartoon Network are reaching more households this year than last—and charging 20% more for ads. Most operations, anchored by recent additions New Line Cinema Corp. and Castle Rock Entertainment, will

## Who Gets What With Turner

*The players negotiating a combination of Time Warner and Turner Broadcasting*

### GERALD LEVIN, TIME WARNER ▶

A Turner deal would put him atop the industry heap—not bad for the old ego. More important, Turner's CNN, Cartoon Network, and TNT would provide valuable programming for Time Warner's cable systems. And TBS's international presence would boost his push overseas.



### ◀ TED TURNER, TBS

Unable to buy a network, he would finally succumb to consolidation in the media business. Not great for the ego. But he would control 10% of Time Warner voting shares, get two seats on the board, and still run TBS. The question: Can Ted work for anyone?

**JOHN C. MALONE ▶** Still a wild card, despite apparent early support for deal. Converting Turner shares to an 8% Time Warner stake presents a possible anti-trust issue. And TCI's movie and sports channels could lose, as Time Warner gets first dibs to Turner programming. The ego satisfaction isn't sure.



# Turner's movie libraries, studios, and cable channels would stretch Time Warner's global reach



# HOW MUCH ROOM IS THERE FOR BARRY?



**DILLER:** Going back to broadcast basics

It wasn't exactly a new idea for Barry Diller. He had first focused on the group of 12 UHF home-shopping stations owned by Silver King Communications Inc. in 1993, when he was peddling zircons as chairman of QVC Inc. Back then, Diller, the man who created the Fox Broadcasting television network for Rupert Murdoch, saw TV's future as interactive. When rival networks

were launched by Time Warner Inc. and Paramount Communications Inc., Diller predicted that neither was likely to survive.

All of which makes Diller's Aug. 25 announcement that he had bought a 20% stake in Silver King and would become its chairman all the more intriguing. What does Diller intend to do with this string of ragtag stations? Create a network. In doing so, the 53-year-old executive says he's going back to the basics of broadcasting. He plans to spend the next year or more creating local programs, sports, and news. "The stations need a voice, and we intend to give it to them," he says.

The plan: create local versions of the hip counter-programming Diller used at Fox to take on the big nets. By going local, he'll hit a market that

is exploding after years of near stagnation. Already this year, local TV ads are up by a robust 9%, figures the Television Bureau of Advertising, which says the likes of Blockbuster and KFC have spent \$3.1 billion in the first six months of the year.

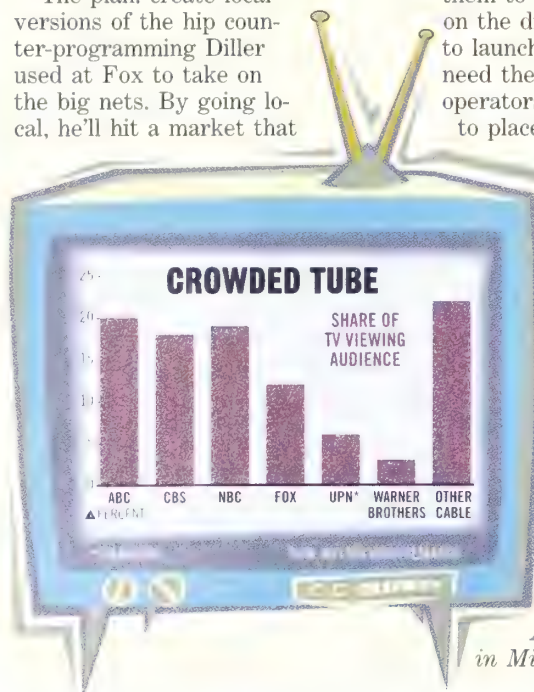
Diller's next step may well be to restructure Silver King's contracts with the Home Shopping Network to allow more time for

other programming. That's where his partner at Silver King, Tele-Communications Inc. and its president, John C. Malone, come in. For Silver King programming, Diller may eventually tap TCI's Liberty Media Corp. unit, which has vast contracts to broadcast sports programming and owns stakes in Lifetime and other cable channels. Diller also intends to develop tailor-made programs for Silver King's markets.

**LOCATION, LOCATION.** But Diller will need a truly magic touch to grab the attention of major-market viewers. Federal rules require cable stations to carry his channels, but to improve his chances, Diller will have to get them to give his stations prime spots on the dial. And when it comes time to launch his network, Diller will need the help of TCI and other cable operators to carry his programming to places where Silver King doesn't have stations.

Skeptics abound. "It's just so much baloney that he can start a network out of those lousy assets he's got," says Dennis McAlpine, an analyst with Josephthal Lyon & Ross. Indeed, some expect Diller to eventually take over HSN, which is 80% owned by TCI. Malone has previously offered him the job. Meanwhile, the man who once sold zircons hopes to turn his string of dowdy stations into something that shines.

By Ronald Grover in Los Angeles, with Gail DeGeorge in Miami, and bureau reports



lk out 50 films a year by 1997. Levin isn't talking, but his rich prod speaks volumes about how much values such assets. Certainly, the ch makes eminent sense for him. e Warner has lofty international amns, and CNN, for one, offers a strong cle for its entry into foreign mar- . "We're trying to do some things nationally, but we're trailing them," one Warner executive.

ist as important, Turner is a master pinning libraries of content into channels. That's what made TNT and Cartoon Network successful. Time ner owns HBO, a strong movie chan- but has fallen behind in developing plementary new networks. More- ; the two companies' varied opera- s would fit together nicely: A merg- ould put Warner Brothers cartoons he Cartoon Network and combine Warner studio libraries with Tur- s. And Warner, Castle Rock, and Line together would own 22% of office market share. "We're in busi- ses that don't compete with each r," says a Turner executive. "The t is, you wouldn't have to eliminate r much at either company."

**L FEUDING.** There are nonbusiness ors, too. The move helps Levin an- r investors who claim he has lacked vation and leadership. It would e Time Warner, with \$18.2 billion ales and a market capitalization of t \$23 billion, virtually unassailable takeover target, even given today's ik-the-bank merger mania. And it ld dilute the power of large share- lers—Seagram Co., for example— ave sometimes disputed Levin's tegy.

looks promising, certainly. But Lev- ould have to show that Time War- can make it work. After all, HBO the Warner cable operations are still ling years after they were joined via ger. Some of Turner and Time War- s businesses don't have obvious fits. l there are no obvious ways to cut s, as Turner could have done by ging together CNN with news opera- s at the CBS network he coveted. he most intriguing part of the deal e how the Turner-Levin combo rs out. Less than a year ago, Turner a National Press Club audience that in was "clitorizing" him by using a e Warner veto on the TBS board to o him from buying a network. Now, ner—who hasn't worked for anyone e taking over the family business age 24—is supposed to answer to in. Scale is important, but ego may win out.

By David Greising in Atlanta, with hael Oneal in Northport, Mich., and ald Grover in Los Angeles



## MARKETING

COLIN POWELL'S BOOK TOUR  
—OR IS IT A WHISTLE-STOP?

The megahype could be a rehearsal for a different campaign

The publishing world is synchronizing watches, waiting for Colin L. Powell's new offensive to begin. No, not Desert Storm II. It's the retired army general's national book blitz.

In mid-September, the hero of the Persian Gulf war will launch a campaign to sell more than a million copies of his memoirs, *My American Journey*. If the tour lives up to megahyped expectations, Powell could launch a budding political career, maybe even a Presidential bid. But even if he doesn't run, Powell will help his publisher, Random House Inc., win a \$6.5 million gamble. That's the reported advance the publishing giant paid the general for his rags-to-battle-ribbons saga. Random House's planned first printing: 950,000 copies, to be sold at \$25.95 each.

**TAPES, TOO.** Industry sources speculate that Random House will have to sell at least 1.5 million hardback copies in the U.S. to turn a profit. That's an ambitious target. But Random House insists the book will earn back its advance at 1 million copies because of revenue from spinoff deals. *Time* magazine is paying upwards of \$175,000 for serial rights, the Book of the Month Club plans to make it a main selection, and publishers in six other countries have signed deals worth about \$1 million. Random House itself will market the audiotape version. "We're pulling out all the stops," says Random House CEO Alberto Vitale.

Precedents for the book bode well. The other hero of the gulf war, Army General Norman Schwarzkopf, sold 1 million hardback copies of his 1993 memoirs—for which he received \$5 million. In comparison, House Speaker Newt Gingrich's book *To Renew America*, published by HarperCollins, is in its sixth printing—with 665,000 copies off the presses. Powell's epic "is going to drown Newt," predicts A. David Schwartz, president of Harry W.

Schwartz Bookshops in Milwaukee. Booksellers nationwide are scrambling to stock their shelves. "We're expecting it to be a best-seller," says Robert J. Wietrak, merchandising vice-president for Barnes & Noble Inc., a 1,000-store chain.

Random House's hopes to ensure that by giving the Powell opus maximum hype. Its campaign includes saturation coverage of Powell on television, including interviews with Barbara Walters, Katie Couric, Jay

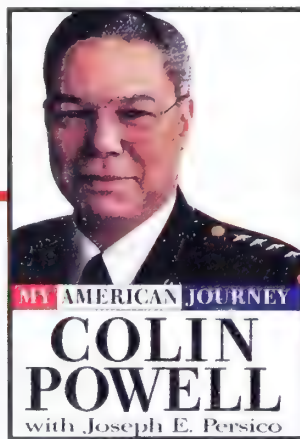
## Book Blitz

The planned publicity campaign for Colin Powell's new autobiography, *My American Journey*

**SEPT. 11** *Time* magazine will issue a lengthy excerpt of Powell's book.

**SEPT. 15** Barbara Walters plans a one-hour special on Powell's story.

**SEPT. 16** Powell launches his 20-city tour, starting in his neighborhood Crown Books store in McLean, Va.



**SEPT. 17** *Parade* magazine schedules a cover story on Powell.

**SEPT. 18** NBC's *Today* show with Katie Couric kicks off a three-day Powell special. CNN's *Larry King Live* also plans a Powell interview.

DATA: RANDOM HOUSE INC.

Leno, and Larry King. "It's the dream tour," gushes Random House publicity director Ivan Held. Print ads will appear in publications ranging from *The New York Times* to *Essence* magazine to *Army Times*. The unusual mix reflects Powell's enormous appeal across racial, economic, and cultural lines.

The five-week frenzied tour begins on Sept. 16 with Powell signing copies at his neighborhood Crown Books store in McLean, Va. His 20-city route includes outlets as diverse as Seattle's hip Elliott Bay Book Co. and a Price-Costco Inc. discount warehouse in Orange County, Calif. At least three African-American bookstores, including

Vertigo Books in Washington, will be on the tour. Random House made its order at least 2,000 copies—an extraordinarily large number—to land a personal Powell appearance.

The key selling point: Powell's military and a national guessing game about whether one of the country's most popular figures has any designs on the White House. The retired general has never declared his party affiliation, much less discussed his political views or ambitions since retiring as chairman of the Joint Chiefs of Staff in 1993. And Random House is making sure any political answers revealed in the book are kept secret until the publication date. Advance copies have been severely restricted, and reviewers have signed nondisclosure forms. "I almost had to sign a blood not to give away details," says one reviewer.

All the attention has Powell's political backers in a euphoric mood. They say the tour couldn't be a better dress rehearsal for a Presidential campaign. W. Ron Evans, a spokesman for the Exploratory Draft Powell Committee for President in Washington, says volunteers will follow the tour with the aim of collecting a million signatures endorsing a Powell Presidential bid. "This gives us the momentum we need," he says. **AGENDA BENDER?** But several Powell associates say they don't believe the tired general has the leverage for public office needed to survive a grueling Presidential bid. Others speculate that his most direct route to the White House is as a Vice-Presidential candidate with GOP front-runner

Bob Dole (R-Kan.), is out of the question. "Let's face it: He'd be signing on someone else's agenda for four years," says Retired Admiral David E. Jeremiah, who served with Powell as vice chairman of the Joint Chiefs of Staff. J. Bruce Llewellyn, chairman of the Philadelphia Coca-Cola Bottling Co., and Powell's cousin, agrees: "I don't think he'd do it."

Will he or won't he? Only Powell knows for sure. But with millions at stake, Random House isn't about to reveal the ending early. The intrigue is the best marketing tool it's got.

By Mary Beth Regan  
in Washington



**PC**  
**MAGAZINE**  
**EDITORS'**  
**CHOICE**

AUGUST 1995  
TI TravelMate 5000  
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**TEXAS  
INSTRUMENTS**



By Joan O'C. Hamilton

# BIOTECH STOCKS: SO SEXY—AND SO SCARY

**F**or more than a decade now, fortunes have been made riding the huge rallies in biotechnology stocks that have routinely followed the industry's periodic dances on the edge of oblivion. Here we go again.

Biotech stocks are up some 40% since late May (chart). The rally began, as have several before it, with a few dollops of good news: In June, a drug from Cephalon Inc. to fight the neurological disorder ALS (Lou Gehrig's disease) showed strong results in late-stage clinical trials, more than doubling Cephalon's market value. Also, Amgen Inc.'s much-ballyhooed gene that makes fat mice skinny caught the public's imagination—despite the lack of any scientific data showing that it will work in people. Meanwhile, regulators are signaling that they'll make biotech drug approvals somewhat easier.

**ANOTHER FALL?** Investors, however, would do well to cast a wary eye on this rebound. The science in most companies is extremely exciting—but a long way from making the leap to becoming consistent, product-spawning technology. Plus, the industry is still a bloated mess. The hundreds of biotech companies in the U.S. will need far too much capital for most to survive long-term.

In short, biotech is inevitably headed for another fall. It's just a question of when. Since the public-capital spigot ran dry in 1993, only a couple of dozen or so outfits have folded, merged, or been acquired. A few large players have placed some big bets—such as Glaxo Holdings PLC's \$533 million purchase of

Affymax Research Institute. But most big drug makers haven't gone on the shopping spree that biotech investors and companies were anticipating. Worse, lots of new companies are entering the market. "This is not a rally the value players are generating," notes Matthew M. Geller, an analyst at Oppenheimer & Co.

In fact, investing pros agree that the rise in share prices is being fueled largely by momentum investors who focus on fast-growing sectors of the market. They fear they have topped out in high-tech stocks and are cycling money into a sector they perceive as having big-return

potential. Many old biotech hands can barely hide their cynicism: "Fresh meat," chortles one venture capitalist about the new players—quickly adding: "Oh, God, don't quote me on that."

The market's on-again, off-again passion for biotech is understandable: As Amgen has proven, a couple of home-run drugs can be a license to print money. Unfortunately, the harsh reality is that the vast majority of seemingly great ideas fail. Diseases that have proven truly intractable, such as cancer, are terribly complex. They defy magic-bullet cures—making home runs few and far between.

For a big drug company with cash and resources, succeeding with 1 out of 10 drugs tested on people is good enough. But in the biotech arena, venture capitalists and entrepreneurs typically exploit overheated capital markets and turn ideas for drugs into 10 separate companies. Each one faces nearly impossible odds.

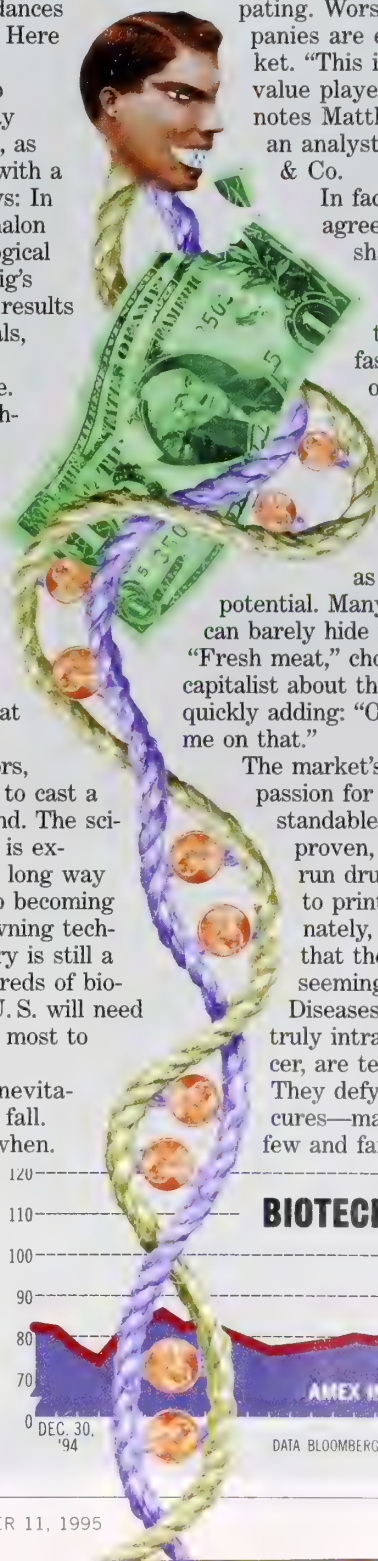
One sure sign the bull run may be ending is the dozen or so startups that have launched initial public offerings. "That's going to hurt the rally," predicts Fidelity Select Biotechnology Fund manager Karen Firestone. "You don't need more companies, and you don't need them competing with existing companies for funds."

**"NEWS FLOW."** Time to sell? May not immediately. Cynicism isn't keeping analysts and fund managers from promoting their favorite stocks. Protein Design Labs Inc. and Cell Therapeutics Inc. have loyal institutional fans promoting them as "comeback" stocks after bad news earlier this year sent those stocks reeling. The newly public Sequa is considered sexy because it's working in the hot field of DNA analysis. Even blue-ribbon names such as Amgen, Chiron, and Biogen are trading at high multiples but could go higher, because they have broad product portfolios.

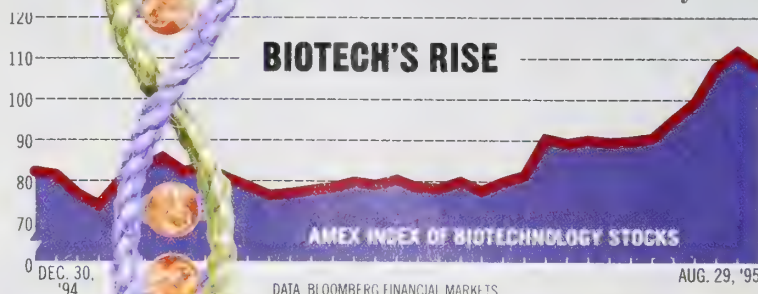
Remarkably, many analysts rely more on "news flow" than cash flow in their forecasts. Their rationale: Within a few weeks, Genzyme Corp. and Chiron will release word on some key trials are going. If they even incrementally positive new it's likely to buoy the confidence of rookie investors who are pouring money into biotech.

Maybe. But if history is a guide, it's only a matter of time before a few high-profile flops will burst the biotech balloon. So investor beware.

*Hamilton tracks biotechnology from San Francisco.*



## BIOTECH'S RISE



DATA: BLOOMBERG FINANCIAL MARKETS



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And while we've long been known for making better things, perhaps from now on we'll be known for making things better.

Jan O. Timmer, President & CEO



# PHILIPS



## MARKETING

# P&G IS STILL HAVING A DEVIL OF A TIME

The rumors of satanism persist

It's not an everyday question at most companies: Do you have any symbols of ram's horns on your products? Yet that's what Procter & Gamble Co.'s public-relations staff is dealing with these days, as they once again fight off rumors that the company is somehow linked to satanism. A satanic ram's-horn symbol, the rumor goes, will soon start appearing on P&G products, bearing the devil's own number, 666.

For P&G, it's the rumor that won't go away. On Aug. 28, the company sued Randy L. Haugen, an independent Amway Corp. distributor in Ogden, Utah, charging that he and unnamed others had made false and defamatory statements linking the company to satanism. This is the sixth suit P&G has filed involving an Amway distributor and the 15th overall since rumors started 15 years ago. But even if P&G wins the case, as it has before, it's not likely that the consumer-products giant will stamp out the rumor.

**ON THE HORN.** Still, P&G may have a smoking gun this time. Someone slipped the company a recording that had gone out over an Amway voice-mail system available to independent distributors who choose to pay for access. As reported in P&G's suit, the message says that P&G's president appeared on the *Phil Donahue Show* and "stated that a large portion of the profits from the Procter & Gamble products go to support his satanic church." The message went on to cite 43 P&G brands by name, from Crisco to Oil of Olay, as well as the by-



now-famous bit about the ram's horn.

Procter & Gamble is clearly unhappy with competitor Amway Corp., the Ada (Mich.) company that sells SA8 laundry detergent, Glisten toothpaste, and other products through 2 million independent distributors. Procter pointedly observes that Haugen is a high-ranking distributor. It also contends Amway hasn't done enough to stop the rumors, though P&G has so far sued Amway distributors, not the \$5.3 billion privately held company itself.

For its part, Amway responds that it "does not condone the spreading of false and malicious rumors against Procter

& Gamble." An Amway spokeswoman says that, at the company's request, Haugen sent out a retraction over the same message system and that Amway hasn't heard from P&G about the rumor in years. Haugen himself wasn't available for comment.

The Haugen suit is only the latest measure Procter has taken to quell the wild story (table). But it's a tale—sometimes with new details—that won't let stake be driven through its heart. In May, P&G was receiving almost 200 calls a day from consumers about it, though the number since has ebbed to 70. About 100 after P&G targeted mailings to churches and media.

Folklorists say the affair's just one example of several "contemporary legends" that focus on business. Remember the one about McDonald's selling worms in its hamburgers? Or the rat in a bucket of Kentucky Fried Chicken?

Why do such stories crop up? The University of Georgia sociology professor Gary Alan Fine, author of a recent book on contemporary legends, notes that many Americans have long mistrusted large companies, whose inner workings are mysterious to them. Adds Bill Ellis, associate professor of American Studies at Penn State University at Hazleton: "There's an implicit belief that for anyone to become really economically powerful, there must be some implicit deal with the forces of evil."

And as Jan Harold Brunvand, a longtime follower of contemporary legends and a professor at the University of Utah, points out, Satan worship at P&G doesn't sound any wackier than much of the stuff on TV talk shows. It's also more durable than the rumor first known as "the Kmart snake," about a shopper who reaches inside a rolled oriental rug and is bitten by a cobra. Unfortunately for P&G, such tales just don't seem to die.

*By Zachary Schiller in Cleveland*

## A FIENDISH HISTORY

Mass marketer Procter & Gamble has been caught up in the longest exorcism on record

**1980** Rumors swirl that P&G is secretly controlled by cult leader Reverend Sun Myung Moon. Other murmurs link P&G's moon-and-stars trademark to witchcraft. P&G issues denials.

**1982** P&G sues six individuals, including an Amway distributor, to quash rumors that an executive confirmed the company's satanic ties on a TV talk show.

**1985** Additional lawsuits; the company

decides to pull its trademark from products.

**1990** P&G sues a Kansas couple, both Amway distributors, for spreading more satanic rumors. It later wins a \$75,000 judgment in the case.

**1991** P&G eliminates from its trademark elements rumored to represent the satanic number 666.

**1995** P&G sues Amway distributor Randy Haugen.

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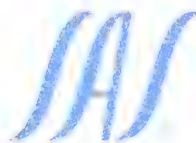
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# HARVARD HONCHOS *Handicapping the top contenders for B-school dean*



## ▼ LEONARD SCHLESINGER

Senior associate dean is leading a major review of the school's curriculum. A risk-taker

**ODDS: 5-1**

**▲ KIM CLARK**  
Highly respected academic chairs technology and operations faculty. Lacks administrative experience

**ODDS: 3-1**



## ▲ JOHN CLARKESON

Led Boston Consulting Group through rapid growth and rejuvenation. The leading outsider

**ODDS: 8-1**

## ▼ MITT ROMNEY

Ran unsuccessfully for U.S. Senate. Boasts solid business credentials but may be deemed too political

**ODDS: 15-1**



## ▲ P. ROY VAGELOS

Former Merck chairman is winning support among alumni. Major drawback: his age, 65

**ODDS: 25-1**

nounced his plan to quit. Schlesinger would bring to the job an unusual real-world credential, having been chief operating officer of the Au Bon Pain Co. bakery-café chain for three years during the 1980s. Light, a thoughtful and candid professor considered to be an unlikely agent for change, has won favor from other faculty who prefer to retain the status quo. Schlesinger and Light wouldn't comment. **"AMAZED."** At the same time, however, the search for a new dean has also produced an unusual list

of outside contenders, all thought to be long shots. Sources say Rudenstine has considered such external candidates as John Clarkeson, president and chief executive of Boston Consulting Group Inc.; W. Mitt Romney, CEO of Bain Capital Inc. and an unsuccessful candidate for the U.S. Senate; Laura D'Andrea Tyson, a University of California at Berkeley economist who chairs the White House's National Economic Council; and even P. Roy Vagelos, 65, former chairman of Merck & Co.

Romney, a member of the Visiting Committee that assesses the B-school every three years, says he hasn't been interviewed for the job. "The school may be considering me, but in my view, it seems that the short list should be exclusively composed of internal candidates," he says. "I would be amazed if the new dean was not an insider." Tyson says she hasn't been approached, and Clarkeson declined comment. Vagelos couldn't be reached.

Whoever gets the job won't have a cakewalk. The new dean will inherit a financially secure enterprise but one considered to be drifting academically, filled with huge, often warring egos. Any candidate will have to lead an overhaul of the school's MBA program, rejuvenate the antiquated executive-education offerings, and squeeze more revenues out of Harvard's considerable publishing operations. All that, plus glad-handing the students each fall.

*By Lori Bongiorno and John A. Byrne in New York, with Mark Maremont in Boston*

## ACADEMIA

# IN THE A-LIST T HARVARD B-SCHOOL

The search for a dean is nearing resolution. An insider is likely

**W**hen Harvard business school's first-year MBAs begin the school year Sept. 7, they will be greeted by a familiar face. John H. McArthur, who last March announced his intention to leave after 15 years as dean, had hoped to be out of a job by now. Instead, he will address students before they set off for classes.

It probably will be one of his last official duties. By September's end, Harvard University President Neil L. Rudenstine is expected to name McArthur's successor. Since March, faculty and alumni search committees have considered a wide range of candidates to lead the world's richest and most powerful business school. Now, Rudenstine has narrowed the search to a handful of finalists from more than a hundred ear-nominees, according to insiders.

**UNION TIES.** A university spokesman says Rudenstine hasn't picked the winner. But the odds-on favorite, according to faculty members and administrators, is Kim B. Clark, a low-profile professor of technology and operations who has won broad support among faculty and alumni. Clark, 46, is Harvard born and

bred, having won his bachelor's, master's, and doctorate degrees in economics there before joining the business school faculty in 1978. He is widely respected for his scholarship—considered a key criterion by faculty members—and is viewed as a potentially articulate spokesman for the school.

Clark, who wouldn't comment, has little administrative experience, though he has been chairman of his department since 1990. That leaves the door open to several other insider contenders: Leonard A. Schlesinger, 43, a dynamic senior associate dean who is leading the school's curriculum changes; Jay O. Light, a popular finance professor and former senior administrator who has long been considered a possible successor; and two of Clark's colleagues in the technology-and-operations area, Robert H. Hayes, 59, and Steven C. Wheelwright, 51.

Schlesinger, the favorite among faculty members who support major changes at the school, took his name out of consideration for the deanship at Dartmouth College's Amos Tuck School of Business shortly before McArthur an-



## INDUSTRIES

### THERE'S GOLD IN THOSE HILLS OF SODA BOTTLES

Buyers of used plastic just can't get enough

**T**he next time you drain that two-liter Coke or a big Gatorade, don't toss the empty in the trash. Yes, it clogs landfills. But these days, "the dirty plastic bottle is worth a lot of money," says James F. Martin, chief executive of recycler Martin Color-Fi Inc.

Martin ought to know. His Edgefield (S.C.) company, like recyclers across the nation, is paying top dollar for all the discards it can find. Demand for polyethylene-terephthalate (PET) containers, which make up 95% of all plastic bottles, is growing by 21% a year, and prices have more than tripled since last November. It's all part of a chain of events involving everything from blue jeans to European food packages.

The frenzy in PET prices is largely because of rising cotton prices, which has driven foreign manufacturers to cheaper cotton substitutes. Early this year, poor cotton crops in China, Pakistan, and India tightened worldwide supplies of the natural fiber, driving U.S. cotton prices in May to \$1.15 a pound. Even at 80¢ a pound recently, it's still 33% costlier than a year ago.

**SQUEEZED.** In response to the runup, Asian mills hiked their use of synthetic fibers, especially polyester. That intensified shortages in the world market for virgin polyester—already in scant supply because of a dearth of the chemical raw material needed to make PET. PET itself can be made into polyester fibers and resins. U.S. virgin-polyester prices spiked 25% in the past 12 months.

The phenomenon had two immediate effects. First, it squeezed apparel makers. Dallas-based Haggar Corp. says higher cotton and polyester prices have pushed its fabric costs up about 5% this year

over last, resulting in added costs of 25¢ to 30¢ a garment. Haggar President Frank D. Bracken says the company has been able to pass along only about 2% of those costs to retailers. Fort Worth-based Williamson-Dickie Manufacturing Co. says retail prices of its jeans have jumped an average of \$2 as a result.

The polyester pinch also drove textile producers into America's used-PET-bottle market, where recycled containers are used to make polyester fibers that are then spun into everything from sweaters to upholstery. As a result, bottle prices shot from as low as 10¢ a pound a year ago to as much as 40¢ last spring, says Clifford J. Christenson, COO of Wellman Inc., the country's largest plastics recycler.

PET-bottle prices have since settled back to around 30¢ a pound as textile manufacturers cut back on purchases in anticipation of new polyester capacity coming on line by yearend. Still, demand for discards isn't expected to wither soon. In recent years, PET has grabbed an increasing share of the food-packaging market from glass and aluminum cans, particularly in Europe. Wellman execs estimate that by 1999, PET bottle use in the U.S. will reach 3.4 billion pounds, an increase of 62% over 1995.

**NEW LIVES:** Over 50% of bottle, that could be recycled aren't

In anticipation of increased demand, recyclers are boosting capacity. Wellman, based in Shrewsbury, N.J., is adding 600 million pounds a year to bring total capacity to more than 1 billion pounds a year by the end of 1998. Martin Color-Fi is boosting capacity 17%, to 175 million pounds, by the end of 1996.

**WASTED WASTE.** For now, all the new capacity is going mostly unused, since recyclers can't get their hands on enough bottles. Jerry Powell, editor of trade journal *Resource Recycling*, figures about half of the industry's existing 1 billion pounds of recycling capacity sits idle.

That's because more than half of the containers still go straight into landfills or incinerators, says Luke J. Schmidt, president of the National Association for Plastic Container Recovery, a group of PET container recyclers. Last year, he says, 565 million pounds of PET plastic containers were recycled. "But the market demand was 800 million pounds. We simply are not doing enough recycling to fill the demand," he says.

Schmidt and others hope the recent runup in prices for used PET bottles will help the recycling effort by boosting curbside collection programs throughout the country. "We're paying more money [for used PET bottles], so cities and states should realize that curbside collections could be very profitable for them," says Martin Color-Fi's Martin.

Some have. Portland, Ore., expanded curbside collection of all plastic containers in July, in large part because a new sorting facility makes collection more feasible. But Bruce Walker, Portland's recycling-program manager, concedes that escalating PET prices is "part of the equation." Portland's recycling effort brings in profits of about \$160,000 annually. Even if such fortune lasts only until the next decent cotton harvest, it's not bad for a pile of dirty plastic.

By Stephanie Anderson  
Forest in Dallas

### PLASTIC PROBLEM

Cotton prices have risen **33%** in a year...



...Causing shirtmakers to use **more** polyester in their blends...



...Causing a threefold rise in the price of recycled plastic bottles used in polyester to **30¢** per lb.



DATA BUSINESS WEEK

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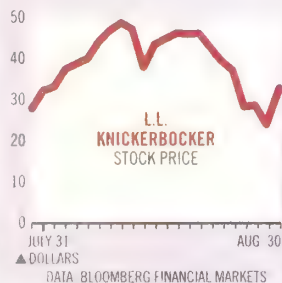
## LEBOW COULD TAKE A PUFF OF RJR

LAST WE SAW, FINANCIER Bennett LeBow's New Valley was emerging from bankruptcy protection last January, shorn of its Western Union money-transfer business but still with \$300 million in cash at the bank. Now, LeBow, a man with some money to spend, is back to do some business: On Aug. 29, RJR Nabisco disclosed that New Valley had received approval from the Federal Trade Commission to buy up as much as 15% of RJR's stock. Analysts say that LeBow is pressuring RJR to spin off its tobacco operations or buy out his Liggett unit, a producer of cheap cigarettes.

## CLOSING BELL

### DOLL-DRUMS

"Hopes and dreams," one analyst called L.L. Knickerbocker, which shot from 5 a share to 48 in six weeks (BW-Sept. 4). Sure enough, Knickerbocker stock tumbled to 23½ by Aug. 29. The next day, though, it soared back to 32½. A surge in sales of the company's tv-pitched Marie Osmond dolls? More likely, say some Wall Streeters, the surge was fueled by anticipation of a 5-for-1 split. CEO Louis Knickerbocker says the roller-coaster ride "has nothing to do with fundamental issues. The company is very strong."



## AN IPO FOR EQUITABLE'S DLJ

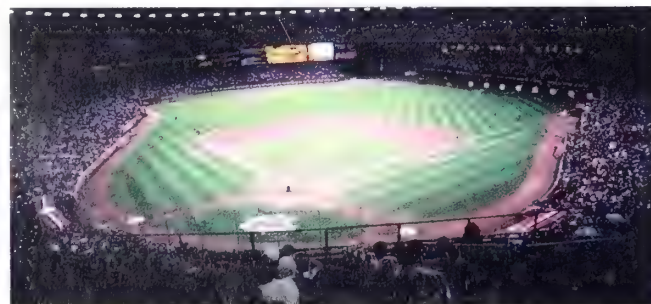
SOME 300 TOP EMPLOYEES AT Donaldson, Lufkin & Jenrette Securities suddenly feel pretty good about their jobs. Equitable Cos. announced on Aug. 29 it would spin off at least 20% of DLJ, its brokerage unit. Good for Equitable: It has been trying to shed DLJ and its volatile earnings for two years, and the IPO is apt to raise \$260 million. DLJ officers, meanwhile, can choose to invest as much as \$100 million of long-term incentives in DLJ units—at an anticipated discount of 33%.

## IBM MAY PULL THE PLUG ON POWERPC

AFTER TWO YEARS OF BUNGLING, sales of PowerPC computers are below IBM's modest hopes. That's why—in the next few weeks, insiders say—IBM will decide whether to pull the plug on its Power Personal Systems Division, which makes PowerPC, folding its products and development efforts into IBM PC Co. or another unit.

## SAY IT AIN'T SO, SAN FRANCISCO

SPORTS FANS, PREPARE ONCE more to be outraged: San Francisco's windswept Candlestick Park, home to baseball's Giants and football's 49ers, appears set to become 3Com Park. That's 3Com, as



**CANDLESTICK:** 3Com wants to be the angel in the outfield

## HEADLINER: PHANTASMAGORIA

### YOU CALL THIS GROWING UP?

In the shadows of a huge mansion, a demon has entered Don's body. Don, understandably upset, plots to kill his wife, Adrienne. She plots to avoid being killed. Murder, rape, and blood ensue. There is no happy ending.

You now know all you need to about Phantasmagoria, a live-action CD-ROM game from Sierra On-Line. The \$69.95 exercise in horror appeared on Aug. 24 and is selling briskly at Egghead Software and Computer City outlets. But not at CompUSA. The No.1 computer retailer, apparently expecting outrage, won't stock it.



"Software comes out all the time. Some we buy; some we don't," the company said in a statement.

Not all software is so gory, though or so... real. Sierra's technology puts actors in a 3-D world, creating some formidable special effects. "It's

time to let computer games grow up and enter the adult world," says Roberta Williams, Sierra On-Line's co-founder. Phantasmagoria's mature rating is displayed on the box, and password option lets parents limit what their kids see. But odds are the kids will figure it out anyway.

By Seanna Browne

in the Silicon Valley maker of networking gear. 3Com is ready to pay up to \$2 million a year to help finance \$25 million in renovations the 36-year-old stadium needs to host pro football's 1999 Super Bowl. The company hopes for increased recognition among consumers, who are increasingly driving PC sales.

## 'GUTS' AND 'PASSION' IN A CFO

AS WAL-MART STORES NEARS a staggering \$100 billion in

sales, it's looking beyond Bentonville, Ark., for top talent. The newest recruit: Ben Franklin Retail Stores President John Menzer, who will join the world's biggest retailer as chief financial officer. With Menzer, 44, Wal-Mart gets "a CFO that really has the guts of a retailer and a real passion for the business," says consultant Burt Flickinger III. Menzer streamlined Ben Franklin's operations, automated warehouses, and focused on craft superstores.

## ET CETERA...

- L'Oréal will pay \$1.4 million to settle charges that it joined a boycott of Israel.
- Boston Scientific will acquire Heart Technology stock worth \$500 million.
- Lockheed Martin will acquire 1,400 top employees of buy company shares.
- AST Research won approval to settle shareholder suits with a \$12.5 million payment.

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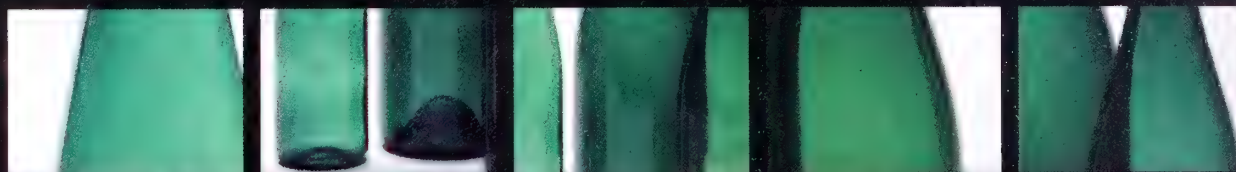




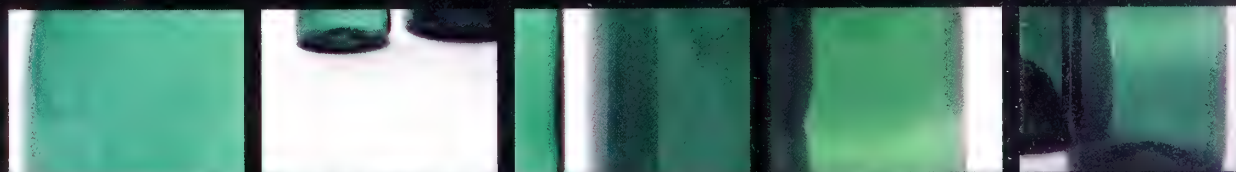
You're on the road. With a client.



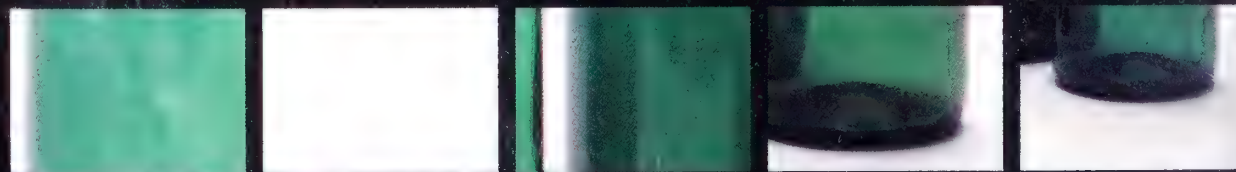
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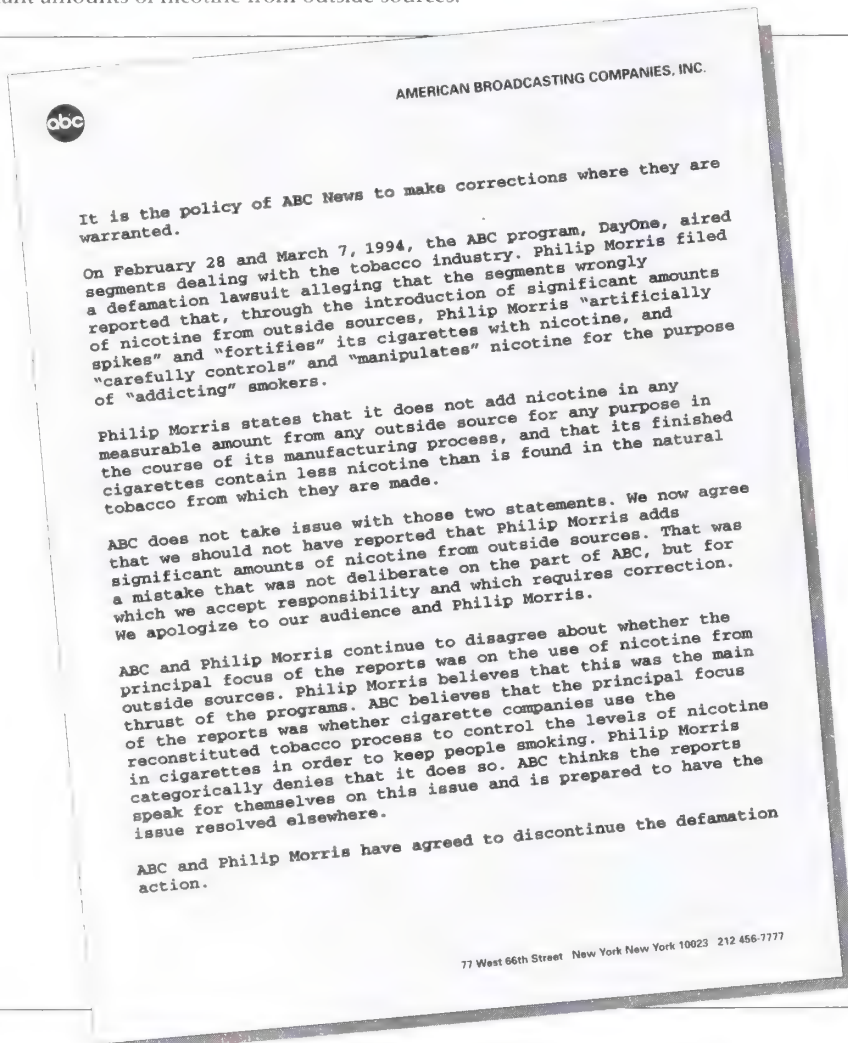


Solutions for a small planet™



# Apology accepted.

The ABC television network has issued the following correction and apology to Philip Morris concerning last year's DayOne broadcasts, which alleged that tobacco companies are "spiking" their cigarettes with significant amounts of nicotine from outside sources:



Philip Morris accepts ABC's apology, which was read recently on the ABC television network.

As for the group of people who eagerly embraced the "spiking" allegation to serve their ongoing crusade against the tobacco industry—we stand ready to accept their apologies as well.

The tobacco industry is subject to relentless attacks. And our responses to accusations like "spiking" are often disregarded by the media and our critics. Here's all we ask: When charges are leveled against us, don't take them at face value. Instead, consider the information we provide, and then—just as importantly—subject the charges themselves to the scrutiny and skepticism they deserve. Fairness and a sincere interest in the truth demand no less.



PHILIP MORRIS COMPANIES INC.

TED BY OWEN ULLMANN

## THE HILL IS TAKING AN AX TO THE TAXMAN

There was one bureaucracy that could always hold its own in Washington's budget wars, it was the Internal Revenue Service. The tax collectors offered Congress a deal it didn't refuse: Give us more money, and we'll squeeze \$3 out of every \$1 we spend. Lawmakers, eager to get the cash without hiking taxes, have poured \$750 million into tougher enforcement since 1990.

Suddenly, that charmed life is ending. After Labor Day, Congress will take an ax to the agency's 1996 budget. Why about-face? All those years of stepped-up auditing didn't deliver the promised cash. Instead, they fueled the public's

frustration with a bureaucracy that symbolizes the intrusiveness of Big Brother. It's not just the antigovernment crowd that's leading the assault. Moderate Republicans—some Democrats—are fed up with an agency that can't keep its own records straight and doesn't answer the phone for two-thirds of taxpayers who call for help.

**ANGRY CUSTOMERS.** Budget cuts may be the least of the IRS's worries. GOP tax reformers are intent on gutting the \$8 billion, 112,000-employee agency. Flat-tax proposals would wipe out the jobs of thousands of auditors and regulation writers.

And even before the tax-reform debate that's expected to reach full steam in 1997, Senator Bob Kerrey (D-Neb.) is pushing the radical notion of privatizing tax collections. "We have to come to grips with an agency that does not have the incentives to make its customers happy," Kerrey declares.

For now, the fight is over auditing. On the block is the Compliance Initiative, a five-year effort to collect \$9 billion in unpaid personal, corporate, and fuels taxes. The IRS got \$405 million extra this year to add 5,000 agents to examine more returns and recover old debts under the program. But the House cut next year's spending by a third, to \$266 million—and the Senate voted to kill it altogether.

The agency charges that only tax cheats will come out ahead. "Our compliance efforts are certainly going to suffer," warns IRS Commissioner Margaret M. Richardson. Adds Donald C. Alexander, agency chief under Presidents Nixon and Ford: "In this Congress, any agency that acts is charged with being 'intrusive.'"

But the IRS's reputation as one of Washington's most mismanaged agencies hasn't helped. On Aug. 4, congressional auditors concluded that the IRS has failed to balance its books for a third straight year. "The IRS has flunked its own audit," complains Senator John Glenn (D-Ohio). Funds that Congress

earmarked for enforcement from 1990 to 1994 were diverted, while uncollected tax debts rose by 80%. Worse, a desperately needed overhaul of 1960s-vintage computers has been hung up in the bureaucracy for years. The result: Two-thirds of the \$23 billion scheduled for modernization will go for patchwork measures to keep the old systems running.

**IRS INC.?** A miffed Senate has backed Kerrey's call for a Commission on Restructuring the IRS to consider such novel ideas as spinning off tax collection to a quasi-governmental corporation. But don't call up

your broker to buy a piece of IRS Inc. just yet. The Clinton Administration opposes Kerrey's commission, and few in the House are ready to turn the agency over to outside control. "The IRS has plenty of overseers already," says departing Deputy Treasury Secretary Frank N. Newman.

But the mere talk of privatizing tax collection—a core role of government—signals the tough days ahead for the IRS. Sensitive to voters' antitax fever and hungry for deficit reduction, Congress isn't about to heed the agency's pleas for more money. The newly trained IRS auditors may indeed be hitting up business soon—for jobs, not back taxes.

By Mike McNamee



**SQUEEZED:** Cuts are hurting the IRS

## CAPITAL WRAPUP

### ARMLESS RADIATION?

A forthcoming study of government radiation experiments on hundreds of Americans in the 1950s has found no evidence of significant physical harm. The surprising findings by a panel of experts convened by the Administration are to be released on Sept. 22. Despite a lack of proven injuries, the U.S. will still honor Energy Secretary Hazel O'Leary's December, 1993, vow to compensate the human guinea pigs—many of them unwitting victims—for unjust treatment. The re-

maining question: How much to pay? Even generous awards may not quell lawsuits by subjects.

### TAKEN FOR A (PLANE) RIDE

► A lopsided deal. That's the news from a General Accounting Office report on a 1988 U.S.-Japan venture to develop a Japanese fighter modeled on the F-16. The agency says that the FS-X project was a boon to Japan's aerospace capability. But while U.S. industry picked up \$1 billion in contracts, it got little of the manufacturing knowhow the feds promised.

### AGENTS ABROAD

► The FBI is going global. Having already hung a shingle in Moscow to help the Russians fight organized crime, the bureau will open a Beijing office in October to join Chinese authorities in combating intellectual-property theft. The effort is a follow-up to last February's U.S.-Chinese accord to crack down on copyright piracy of movies, cassettes, CDs, and computer software. Illicit Chinese goods cost U.S. companies almost \$1 billion in lost sales annually.



JAPAN

# HERE COMES HASHIMOTO

The abrasive politician may soon ascend to Japan's pinnacle

**W**ith his slicked-back pompadour, 1950s sideburns, and caustic wit, Ryutaro Hashimoto has always played the maverick in consensus-loving Japan. Around the conservative Liberal Democratic Party, Hashimoto even became known as Mr. Pamado, after the Japanese word for hair gel, because of his image as a smooth political operator. Most recently, the International Trade & Industry Minister won celebrity status for his abrasive negotiating style in this summer's tumultuous U.S.-Japan auto talks.

Now, Hashimoto, 58, is on his way to becoming Prime Minister. In a surprising development on Aug. 28, Hashimoto effectively won the leadership of the conservative LDP when incumbent President Yohei Kono, who is also Deputy Prime Minister and Foreign Minister, announced he would not fight for the job in a Sept. 22 party leadership vote. With his victory as party president virtually assured, Hashimoto is setting his sights on reviving Japan's biggest political party and becoming the most assertive Prime Minister since the war.

His ascent would help Japan's economic recovery, which is already getting an assist from a recent string of financial bailouts. But more broadly, Hashimoto's leadership would expand Japanese influence in Asia while creating even testier trade relations with the U.S. (table). In all these areas, he would be able to exercise real clout. One reason is that, after a long series of Prime Ministers with little grip on the mechanisms of power, his background as MITI's

czar and as Finance Minister would give him a shot at exerting a measure of influence over elite bureaucrats. The son of a wartime Cabinet minister, he has strong bases of support in many industries and among right-of-center political groups.

The political shakeup won't happen overnight. With Hashimoto as LDP leader, the next step is expected to be a major upheaval within the wobbly three-party coalition government of Socialist Prime Minister Tomiichi Murayama, of which the LDP is the largest bloc. The coalition has already signalled its intention to hold general elections in early 1996. The expected winner is the LDP, which has been forced to share power with the Socialists since a series of corruption scandals ended its 38-year reign in 1993.

**LONG COATTAILS.** Hashimoto's popularity is the ticket the whole LDP could ride back to uncontested power. A recent poll by *Nihon Keizai Shimbun*, Japan's economic daily, named him as the electorate's first choice for Prime Minister, eclipsing so-called reformers who bolted from the LDP. "If the LDP has a popular leader like Hashimoto, chances are they will win," concedes Yoshio Terasawa, an Upper House Diet member of the breakaway New Frontier Party.

That's not to say Hashimoto is a sure bet. Although he has vowed to sever all links "between politics and dirty money," his opponents are sure to make an issue of Hashimoto's ties to LDP faction leaders such as ex-Prime Minister Noburo Takeshita. Then, there's Hashimoto's fiery oratory style. It



**CLIMBER:** Hashimoto has grabbed control of the

played well in U.S.-Japanese trade talks, but could be a liability on the broader world stage. "When he becomes premier, he will adjust his style to become softer, more serious," predicts party honcho Koichi Kato, chairman of the LDP's Policy Research Council.

For now, Hashimoto has vowed to work with Murayama, given the need to push a \$10 billion economic stimulus package through the Diet by year's end and to host November's Asia-Pacific Economic Cooperation forum in Osaka. But Hashimoto's instincts couldn't contrast more with the Socialists'. As Murayama issued a heartfelt apology on the 50th anniversary of Japan's defeat, Hashimoto



## SHIMOTO BECOMES TIME MINISTER...

**SE ECONOMY** He would be more inclined to take steps to stabilize Japan's financial sector, regulate overall growth, implement spending measures and regulatory steps.

**ATIONS** He would be more assertive, insisting that Tokyo and the U.S. negotiate as equals. This could probably spark tougher negotiations.

**ELATIONS** He would accelerate Japan's engagement with Taiwan and Southeast Asia, including Cambodia, but his hawkish views on relations with China and Russia.

**Y POLICY** He would promote Japan's membership in the U.N. Security Council and forge a more assertive Japanese foreign policy that include a military dimension.

DATA: BUSINESS WEEK



**SEARCHING FOR ARMS IN CAMBODIA:** Hashimoto seeks to boost Japan's role overseas

aid a controversial visit to Tokyo's Meiji Shrine, the venerated memorial to Japanese war dead. Hashimoto is president of the 1 million-plus member Japan War-Bereaved Families Assn., a group that believes Japan fought an honorable war of liberation in Asia.

Unlike Murayama, Hashimoto aims to see Japan play a diplomatic role commensurate with its economic power. He squarely behind Japan's bid to gain a permanent seat on the U.N. Security Council. And Hashimoto favors sending Japanese troops and security forces on U.N. peacekeeping missions abroad.

Hashimoto would also be more sympathetic to Corporate Japan's calls for corrective measures to tackle the economy's post-bubble ills. For example, he's already pushing for an easing of securities transaction and property taxes. It's in sharp contrast to the Socialists, who have been loath to bail out executives and property speculators whom many perceive as greedy opportunists.

Securities Inc. analyst Cameron Mitsuetsu thinks a Hashimoto victory would be bullish for stocks. One reason:

Hashimoto has set an ambitious goal of driving down by the year 2000 Japan's massive current account surplus to roughly 1% to 2% of gross domestic product, from almost 3% now, in order to bring the superyen back to earth.

Hashimoto, as former Finance Minister, also has the right credentials to accelerate Japan's cleanup of its financial system. After years of denial, the Finance Ministry and the Bank of Japan are beginning to move in that direction. A month after dispatching truckloads of yen to handle a \$1 billion-plus deposit run against Tokyo's biggest credit union, Cosmo Credit Corp., authorities on Aug. 30 swooped down to rescue two big Osaka-area financial institutions at a cost of more than \$10 billion.

But the tricky task of streamlining the financial system is just beginning,

fed up with U.S. trade demands. Nevertheless, White House officials feel Hashimoto is a guy they can do business with. Says a senior Clinton Administration official: "He talks loud and carries a big stick, but he is willing to negotiate and reach agreements in the end."

Still, Hashimoto is sure to keep taking a tough line on trade disputes with the U.S. over everything from semiconductors to film to telecommunications equipment. Nor will Washington likely appreciate Hashimoto's greater focus on Asia. He and other members of his increasing nationalistic generation

## The political shakeup won't happen overnight. Elections may come in early '96, and with Hashimoto as leader, the LDP would likely win

and Hashimoto's ascendancy would help guide it. "He speaks the Tokyo language" of elites, says Fuji Research Institute Corp. Chairman Toru Kusakawa, "Hashimoto is a man who can lead."

Perhaps the biggest imponderable about Hashimoto is how he would deal with the Americans. He proved himself a resolute infighter during acrimonious auto trade talks in June, which played well with a Japanese public increasingly

hope to use Japan's wave of investment and development aid flowing into the region to help Japan Inc. extend its tendrils over these blooming markets.

In a Japan increasingly edgy about its future, Hashimoto's brash style touches a powerful current. Should his political ambitions be realized, the world will confront a far different style of political discourse from Japan in years ahead.

By Brian Bremner in Tokyo



## CHINA

# A THAW DOESN'T NECESSARILY MEAN SPRINGTIME

Bones of contention will mar Sino-U.S. relations for years

After a frigid summer, Sino-U.S. relations are warming. China released U.S. human-rights activist Harry Wu, approved several deals with U.S. companies, and said it would send its ambassador back to Washington. For Washington's part, First Lady Hillary Rodham Clinton went ahead with plans to attend a U.N. conference on women, and the White House tentatively agreed to a presidential summit in October.

But the U.S. and China have anything but a smooth road ahead. On such issues as China's entry into the World Trade Organization, claims in the South China Sea, and overseas arms sales, the interests of Beijing and Washington clash sharply. The emotionally charged issue of Taiwan, which holds its first direct presidential elections in March, could be a flash point as Beijing worries about a possible drift toward independence.

For now, Beijing seems to have concluded that the downward spiral in relations has gone far enough. The immediate incentive: prospects of a summit between President Bill Clinton and Chinese President Jiang Zemin. That would greatly burnish Jiang's stature at a time when he's embroiled in a power struggle to succeed the ailing Deng Xiaoping. "A Jiang visit to the White House is a very important symbol in China," says a Beijing legal scholar.

Another reason for the apparent zig-zagging may be that China's leaders believe they've already accomplished some key goals with threatening military exercises near Taiwan. Beijing seems to have gotten its point across as Republicans such as U.S. House Speaker Newt Gingrich back away from pro-independence rhetoric. The Clinton Administration may make its policy clearer with a major

address explaining that it is not trying to "contain" China. After months of delay, meanwhile, Beijing is considering approval for the Administration's nominee for ambassador to China, former Tennessee Senator Jim Sasser.

Chinese leaders also seem to agree that stable relations are important economically. America buys 30% of China's exports, and Beijing wants continued

each side can go in improving relations. With its trade deficit with China expected to approach \$40 billion this year, Washington is determined not to let China into the WTO unless it opens its market more. Inside China, power brokers have clearly become more conservative in the year or so since Deng, 91, became too feeble to make key decisions. In the past, he would step in to break a foreign policy deadlock. But few other leaders can face down the military on national security issues.

The People's Liberation Army fears that Taiwan's native-born President Lee Teng-hui will promote independence. Western military analysts expect China to hold more maneuvers off the Taiwan coast. The military has reasons to keep the heat on. The PLA watched the U.S.

and France sell military hardware to Taipei. And it grew angrier as Lee traveled throughout Southeast Asia and then to the U.S. To the generals, that proved the "soft" approach over Taiwan wasn't working. The issue gives them "a sense of mission, which they've been looking for since the end of the cold war," says military analyst Tai Ming Cheung. Kim Eng Securities in Hong Kong.

**ISLAND CLAIMS.** With Beijing claiming sovereignty over the disputed Spratly Islands in the South China Sea, the military also sees a good opportunity to modernize its naval and air force in the name of defending the area. China has backed down in the South China Sea, at least temporarily. But the long-term risk of confrontation with Taiwan remains

high. That could sour the reconciliation with Washington.

No doubt, it's in everyone's interest for cooler heads to prevail. That could create a climate where the two sides can zero in on the tough issues that still confront them. But the diplomatic work ahead is daunting. Says Carl Walter, director of CS First Boston Corp. Beijing office: "The Taiwan issue isn't going away, and it will inevitably involve the U.S." That means relations between Washington and Beijing could still turn dangerously nasty at a moment's notice.

*By Joyce Barnathan in Hong Kong with Dexter Roberts in Beijing and Amy Borrus in Washington*



### KEY PLAYER

For now, at least, the army can sway the national

U.S. investment and technology. By making a show of throwing big-ticket deals to European companies, it risked alienating Corporate America, its most potent lobby in Washington.

Deals are, in fact, popping again. Ford Motor Co. announced plans to invest \$40 million in a minivan joint venture, American International Group got approval to open the first foreign insurance office in the southern city of Guangzhou, and Lockheed Martin Corp. landed a \$100 million contract to build a communications satellite for China. Prospects for Boeing Co.'s jumbo jets also have brightened.

There are limits, however, to how far

Everyone  
thinks Unisys  
is just a computer  
company.

Everyone's wrong.



## ITALY

### THE BRAVO COULD PUT FIAT IN OVERDRIVE

The carmaker bets billions on another foray into midsize cars

European drivers usually associate the Fiat name with one type of car—the snazzy subcompact that can navigate the melee of a Paris boulevard or the narrow streets of Tuscan villages with equal ease. Now, capitalizing on the success of its latest subcompact, the Punto, the Italian auto giant wants to elbow its way into Europe's midsize market, the Continent's most crowded and competitive segment.

It's hardly a sure thing. An earlier generation of midsize Fiats barely budged from the showroom, and rivals are rolling out new cars, too. But Fiat is betting on its new Bravo and Brava models, launched on Aug. 29, to solidify its comeback from a \$1 billion loss in 1993. Fueled by a devalued lira and the hot-selling Punto, Fiat turned a \$612 million profit in 1994. Sales are strong this year, but margins are wider in midsize cars, and Fiat needs a new winner before the Punto loses momentum. Hence the Bravo, a roomy two-door hatchback, and the Brava, a sedan with four passenger doors and a rear door that's a cross between a hatchback and a trunk. Says Fiat Managing Director

Paolo Cantarella: "We are adding two vital pieces to our growth strategy."

The midsize market is the only segment that has withstood Europe's three-year recession, gaining 4.1% in sales since 1992, to 3.6 million last year. That's because the cars have attracted budget-squeezed families looking for the right mix of price and space. But the segment is dominated by such best-sellers as GM-Opel's Astra and the Volkswagen Golf, which contend for the market's top position. Fiat stumbled badly when it tried to break into midsizes six years ago with the Tipo. After a strong start, Tipo sales plummeted to just 46,000 last year, as drivers rejected its ho-hum styling and technological flaws. "The Tipo was never considered a car of comparable standing to the likes of the GM and Volkswagen," says John Lawson, an auto analyst at DRI/McGraw-Hill.

**MORE POWER.** But Lawson and others believe that Fiat has learned from its mistakes. The Bravo and Brava, designed and engineered in Fiat's Cassino plant in a record 32 months, are variations on the Punto theme of technological sophistication and sleek styling. The

twins boast Fiat's brand-new five-cylinder engines to offer drivers the power of a larger car. Other features include sound-

proofing to muffle exterior noise, the latest in easy-to-use controls, and sleek, rounded body. Analysts estimate that the weak lira will permit prices from \$13,750 to \$20,600—some \$2,000 below the competition.

If Bravo and Brava take off this fall, they could help double Fiat's 1995 profits, which are surging anyway thanks to the Punto. Next year, Fiat plans to further widen its line by launching the A178 "world car" for the low budget and rough roads of developing markets.

A flop, of course, would be disastrous. Fiat has spent \$2.5 billion developing the Bravo and Brava and their engine and launching a marketing blitz. Fiat hopes to sell 100,000 by the end of the year and 350,000 in 1996. VW sells about 750,000 Golfs in Europe a year.

**SALES SLUMP.** Market conditions and the competition could still thwart Fiat. Although the midsize category has been resilient, overall car sales in Europe slipped 3.3% in July after government-sponsored sales incentives in France and Spain expired in June. The stock of unsold cars is on the rise. Carmakers from Peugeot to Nissan to Opel are all expected to introduce new midsize models.

Fiat also has to worry about Renault, which launches its midsize Mégane sedan on Sept. 5 to replace the aging Renault 19. The sedan offers the same styling and rear-door feature as the Bravo, and analysts say Renault's established presence in the midsize segment might give it the upper hand. "Even the Bravo/Brava are good products. German or a French consumer might still think twice about buying a serious car from Fiat," says auto analyst Carl Di Grandi of Paribas Ltd. in London.

The first Bravo and Brava owners will be hitting the autobahns and avenues in mid-September. That road test could shake up the entire European auto industry—or throw Fiat into reverse.

By Christina Bennett in Turin



THE BRAVO COULD FACE FIERCE COMPETITION FROM RENAULT'S NEW MEGANE SEDAN

### The Market Fiat Wants to Crack

|                    |                                                           |
|--------------------|-----------------------------------------------------------|
| <b>CAR TYPE</b>    | Midsize, including sedans, coupes, and hatchbacks         |
| <b>PRICE RANGE</b> | \$15,000 to \$24,000                                      |
| <b>MARKET SIZE</b> | 3.6 million cars sold in 1994                             |
| <b>THE PLAYERS</b> | VW Golf, Opel Astra, Ford Escort, Peugeot 306, Renault 19 |
| <b>NEW ENTRIES</b> | Fiat Bravo/Brava, Renault Mégane                          |

DATA BUSINESS WEEK



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# UNISYS



EDITED BY ROSE BRADY

## JORDAN WON'T BE BURNING ITS BRIDGES TO IRAQ

It was music to Washington's ears. When Jordan's King Hussein went on television on Aug. 23 calling for an end to "suffering" and the start of a "new dawn" in Iraq, Clinton Administration officials applauded the King's shift away from Iraq's Saddam Hussein. The speech followed the King's decision to grant asylum to two Iraqi military officials, Saddam's sons-in-law, who defected in early August. Declared an Administration source: The King's actions will "inevitably have an impact on the dynamics of the region."

But the consequences are unlikely to be as dramatic as the U.S. hopes. Although King Hussein is clearly distancing himself from Saddam, Jordan's economy is still heavily dependent on Iraq. To truly isolate Saddam as the U.S. would like, Jordan would have to sever its economic links with its neighbor.

**TINY STEPS.** That's impossible unless the U.S. and its allies in the region move decisively to bolster Jordan's economy. For a host of reasons, including U.S. Congressional opposition to increased foreign aid, that's likely to happen only through tiny steps rather than sweeping moves. Says Anthony H. Cordesman, a Middle East expert at Washington's Center for Strategic and International Studies: "The pressure is growing on Saddam, and Jordan is moving more firmly away from Iraq. But the policy will be slow."

It would be political suicide for King Hussein to abruptly cut his economic ties with Iraq. Jordan receives nearly all its oil from Iraq and sells the country one-third of its exports, for revenues of nearly \$350 million annually. More than 200 Jordanian companies depend on Iraq as their principal market. They lost their markets in Kuwait and Saudi Arabia after Jordan refused to back the anti-Iraq coalition in the gulf war.

Under U.N. sanctions against Iraq, Jordan is allowed to export humanitarian items to its neighbor, including medicines,

hygienic products, foodstuffs, and household oils. It is supposed to monitor trade to prevent industrial products from seeping through the embargo, but controls are weak. "We're relying on Iraq," says Ali Husri, vice-president of Hikma, a \$40 million pharmaceutical company that receives 15% of its revenues from Iraq.

**MINOR SUCCESSES.** The U.S. is trying to persuade Kuwait and Saudi Arabia to boost ties with Jordan. On recent diplomatic missions, U.S. officials came away with minor successes. Kuwait said it would sell crude to Jordan, while Saudi Arabia has promised a summit between King Fahd and King Hussein.

But that's only a beginning. Kuwait and Saudi Arabia would have to supply the 70,000 barrels a day in oil that Jordan now receives—at half the market price—from Iraq. They would have to open their economies to Jordanian products. And the U.S. would have to assure Jordan that the peace process would soon lead to more open markets and trade with Israel.

But Congress would surely nix proposals for more aid to Jordan, even for the key goal of isolating Saddam. Budget fights in Congress have already held up Clinton's proposal to forgive \$275 million in Jordanian military debt. The package will be considered again in September.

So the U.S. shouldn't count on King Hussein's recent moves shaking up geopolitics in the Middle East overnight. To be sure, Saddam has been weakened. He may soon have to face an opposition campaign waged from outside the country. But the 8-year-old dictator still has tight control of the nation's repressive security forces and its media. And he knows that Jordan needs Iraq's markets just as much as Iraq needs Jordan's until the U.S. moves more assertively to spur change.

By Kirk Albrecht in Amman  
and Stan Crock in Washington



**IRAQI OIL:** Jordan gets 70,000 barrels daily

## GLOBAL WRAPUP

### CHASING DICTATORS' CASH

► The Philippines government is close to recouping the "Marcos millions" allegedly stolen by former dictator Ferdinand Marcos and salted away in Swiss banks. Zurich's chief prosecutor, Peter Cosandey, ruled on Aug. 28 that an estimated \$500 million can be transferred to Manila unless his decision is challenged by Sept. 16.

Now it may be open season on dictators' alleged cash hordes hidden in Switzerland. Haiti is seeking \$260 million from accounts of former President

Jean-Claude Duvalier. The Central African Republic wants funds in accounts of former emperor Jean Bédel Bokassa. Even Saddam Hussein may have worries. According to Iraqi exiles, Iraq's Ambassador to the U.N. in Geneva, Barzan al-Tikriti, Saddam's half-brother, controls family cash in Switzerland. He is rumored to be siding with Hussein Kamal Hassan, Saddam's son-in-law who defected to Jordan.

### CANADIAN RALLY

► The Canadian dollar hit an 18-month high of 74.68 U.S. cents on

Aug. 28, amid mounting optimism that Canada will remain united. Quebec Premier Jacques Parizeau has launched a campaign to promote Quebec sovereignty before a key referendum expected this fall. But to build support, Parizeau has softened his definition of sovereignty. He's assuring Quebecers that they could vote for "sovereignty," yet retain an "economic association" with Canada. Still a recent poll suggested that voters would narrowly reject sovereignty if a vote were held now. That kicked off the dollar's surge.



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thought of  
everything.



Chapter One



WITHOUT  
ANTI-LOCK  
BRAKES

WITH  
ANTI-LOCK  
BRAKES

Anti-lock  
brakes help you  
brake and steer  
your way out  
of danger. And  
now we made  
them standard  
equipment on  
most models.



We moved the wheels  
farther apart, front and rear.  
Which gives the new  
Caravan even more stability.



Ultra-high strength steel door beams and front and rear crumple zones  
are part of the new Caravan's energy management system, which helps  
protect occupants from the force of an impact.



The new  
Caravan  
offers a  
personal alarm  
system that you  
can turn on or  
off by remote  
control.



It's so easy  
to deploy the wheels  
on our rear benches,  
you can do it with  
one hand, tied behind  
your back.

There's room for 28 2x4s  
under the back seats. Plus  
we made the liftgate easier  
to lift and to close.



The wheels on our Easy Out Roller Seats™ pop down like landing gear.

We know safety is important to you. So to help protect you and your family, the new Caravan exceeds 1998 car safety standards.

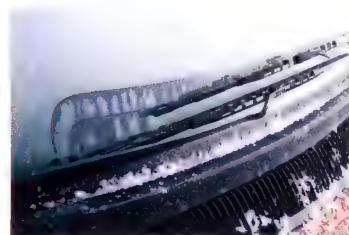
The new Caravan thoughtfully comes with both a driver and a front passenger airbag, standard equipment.

There's 34 cubic feet more room inside the new Caravan. You'll enjoy discovering here we put it.



Our new single buckle system makes our available integrated child safety seats more convenient for parents.

It's a perfect foursome. And since the new Caravan comes in two sizes, it fits families of all sizes.



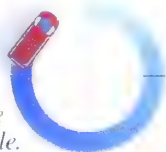
Here's a new option – heaters for the front and rear wipers that help melt away ice and snow.

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We offer a sliding door on the driver's side, as well.



A significantly smaller turning circle makes the new Caravan more maneuverable.



- Steel patch
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For more options, select a pair of our Quad Command Seats. Because they fold flat, you get a set of tables in the bargain.



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Just as original as the original.<sup>TM</sup>

# THE GROCERY CART IN YOUR PC

Shoppers—mainly women—love Peapod's online food-buying service. But will it ever turn a profit?

**W**ith two young daughters and a 60-hour-a-week job, Beth Mansfield of Libertyville, Ill., doesn't have time to squeeze the cantaloupes at her local supermarket. Up until six months ago, the frazzled 42-year-old owner of a sports-equipment franchise would make late-night runs for the bare necessities. But now, when the cupboard is bare, all it takes is a few computer keystrokes—and the problem is solved.

Mansfield's secret is Peapod, a five-year-old online grocery-shopping service based in Evanston, Ill. While many computer shopping ventures have fallen flat, Peapod has built a loyal following of more than 10,000 households in Chicago and San Francisco. It's currently negotiating a partnership deal that will allow it to enter Boston early next year.

Although still tiny, Peapod has turned much of the conventional wisdom about online shopping on its head. In a recent survey, consumers say they won't pay extra for the privilege of shopping online. But Peapod's customers fork over a \$29.95 startup fee, a \$4.95 month-service fee, plus \$6.95 and 5% of their grocery total per order. The service recently raised those prices with scarcely a ripple of protest.

**100% RETENTION.** And Peapod's demographics are the mirror image of those of most other online services, where 90% of shoppers are male. Almost 75% of Peapod's shoppers are women—an important skew, since women usually make household buying decisions. And while most other online-shopping services have trouble retaining their customers, Peapod has kept almost 80% of the people who have tried it. "If you use an online service that answers a need, people will fall in love with it on



## Peapod's Virtual Supermarket

- Items can be chosen from menus organized by broad category (snacks), narrow category (pretzels), or brand name (Rold Gold)

- Items can also be sorted by cost per ounce or by what's on sale to figure out the best buys

- Shoppers can add comments to their orders ("Get only ripe tomatoes") and tell Peapod's in-store shoppers whether they'll accept substitutes

- Shoppers can see a running tally of their bill as they compile their shopping list

- The service takes coupons and accepts credit cards, checks, or online payments

their own," says Tim Dorgan, Peapod's executive vice-president.

Peapod is the brainchild of Andrew Parkinson, 37, and his brother Thomas, 35, both veterans of Procter & Gamble. Andrew says sales will top \$20 million this year. But Peapod has yet to turn a

profit, and some online shopping experts doubt it ever will—unless it raises prices dramatically to pay for the high level of service it provides. Peapod, with 450 employees, hires its own shoppers to fill orders and its own drivers to make deliveries. Software development is another big expense. This fall, for example, the company expects to offer those customers who are worried about fat, sugar, or salt the ability to sort groceries by nutritional content. Andrew says that, once Peapod can spread its high fixed costs over a larger customer base, it can make money without rais-

ing rates or cutting services.

**TAKEOFF POINT.** For now, the company is using cash from equity investors to fund its expansion plans. Peapod has attracted the interest of big media players such as Tribune, Ameritech, and most recently, Providence Journal, all of which have purchased minority stakes in the privately held company. Although they won't disclose the size of their investments, all three have cable interests and think Peapod could someday make the jump to interactive TV. Beyond that, they're betting that the online grocery business is about to take off. In June, Microsoft Chairman William H. Gates III startled a group of top food retailers by predicting that one-third of food sales would be handled electronically by 2005.

That would be a huge shift in the highly competitive, \$400 billion U.S. grocery business. Currently, fewer than 1% of groceries are bought from home—and mostly by phone rather than computer. "This industry is very much in its infancy," says Fred Schneider, executive director of food-industry research at Andersen Consulting. "The important thing Peapod is showing is that consumer demand is out there."

How does it work? Peapod's supermarket partners zap it daily price updates on more than 18,000 items, from laundry detergent to lettuce. At-home shoppers can peruse whole categories, much as they would in a store, or jump straight to their personal shopping list. Since items are broken down by cost per ounce, it's easy to comparison-shop. Customers can tell Peapod's in-store



shoppers whether they will accept a substitute if the preferred item is out of stock. B. Joseph Pine II, a Ridgefield (Conn.) marketing consultant, says this sort of customization binds customers to Peapod's service. "They're enabling the software to remember you. That makes it more difficult for you to go somewhere else," he says.

Once an order is complete, shoppers select a next-day delivery time. Peapod then forwards the order to the nearest participating grocery store. In Chicago, it's a Jewel/Osco; in San Francisco, it's a Safeway. The stores may lose something in impulse purchases, but they gain in volume. Orders are filled by Peapod employees, checked out at special Peapod counters, and taken to a holding area where items are kept frozen or refrigerated as needed. Then, the groceries are picked up and delivered by another set of Peapod employees. For busy, dual-income families, Peapod can cut the weekly shopping trip from a couple of hours to just a 20-minute session at the keyboard.

**FEW RIVALS.** Besides saving time, Katherine M. Howard, a 33-year-old computer systems manager and mother of two, says Peapod makes her a better shopper because she makes fewer impulse purchases, compares prices more easily, and uses more manufacturers' coupons, which Peapod credits to her bill. "It pays for itself in what you don't buy. I love it," she says.

Given the size of the potential market, it's surprising that Peapod has so few competitors. Of the handful out there, none are following the same game plan. Shoppers Express in Bethesda, Md., lets consumers in 40 markets including Miami, Seattle, and Washington, order groceries through America Online, but it acts more as a middleman. Grocery-store employees fill the orders and a local courier delivers them. No prices are quoted, and no comparison shopping is possible. Another Bethesda company, Shopping Alternatives Inc., provides grocery-shopping and delivery services in 10 cities through partnerships with chains such as Cub Foods and WalMart. But the service isn't online yet: Customers pick up a floppy disk or catalog with estimated prices.

For all its high-tech razzle-dazzle, Peapod's greatest strength may be the care it takes in delivering exactly what people want when they want it. "You tell them you want four green bananas and two ripe ones, and that's what they'll give you," says Mansfield. With service like that, lots of other time-pressed consumers may steer their shopping carts for the supermarket in cyberspace.

*By Susan Chandler in Chicago*

## People

### INNOVATORS

# MERCEDES' MAVERICK IN ALABAMA

An unlikely exec leads a radical, high-stakes experiment

One spring day in 1994, two Mercedes executives, Roland Folger and William Taylor, clung to a narrow ledge above the raging Aache River in the Austrian Alps. Below them, their handmade raft bounced crazily in the icy current. Despite their neoprene wet suits, the men shivered as they waited for companions to lower a rope from the cliff above.

A wilderness adventure gone awry? Nope—just a team-building exercise cooked up by the men's boss, Andreas Renschler. The lanky, 37-year-old Renschler is helping to shake up Mercedes-Benz as part of the ongoing transformation of the once-ponderous German luxury carmaker. As president of Mercedes-Benz U.S. International Inc., which in 1997 will start making the company's first mass-market sport-utility vehicle, in Vance, Ala., Renschler is overseeing Mercedes' most radical experiment yet with manufacturing and engineering techniques.

**"A LAB."** At stake in the more-than-\$1 billion project is Mercedes' ambition to position itself as a cost-competitive global manufacturer. The Vance factory will be Mercedes' first big foreign plant, and the All Activity Vehicle (AAV) to be made there will be its first product aimed mainly at a foreign market. The venture is also the carmaker's boldest gambit yet to apply CEO Helmut Werner's new cost-driven ethic. "The AAV is a lab for us," says Dieter Zetsche, a managing director. "It has to be very successful."

Renschler's youth makes him an unusual choice for such a critical job. It's also a key reason Werner tapped him: He's not steeped in the Mercedes culture, where slavish dedication to engineering excellence drove product costs off the chart. Says Zetsche: "You don't need to know all the paths and solutions of the past to find new ways. Sometimes it's better if you don't."

Some observers think Renschler is in

for a rough ride. As Werner's assistant in the early 1990s, he helped plan the current turnaround and became known as a deft manager and a creative problem solver and idea generator. He also planned strategies for light trucks in Europe and Latin America and ran the feasibility study for the AAV. Still, he has

#### ANDREAS RENSCHLER

##### BORN:

March 29, 1958, Stuttgart

##### DEGREES:

Economic engineering,  
Technical Academy, Esslingen  
Business administration,  
Eberhard Karls University,  
Tübingen

##### CAREER:

First job: Bank apprentice  
1983: Management trainee  
at mechanical engineer  
Trumpf Maschinenbau  
1986: Joined Hewlett-  
Packard GmbH  
1988: Joined Mercedes-Benz  
1993: Named President,  
Mercedes-Benz U.S.  
International Inc.

been at Mercedes only six years, has little operating experience, and has never launched a product. Moreover, his task is daunting. While Japanese transplant typically copy plants back home and assemble existing models at first, Renschler will have to simultaneously debug product, a manufacturing process, and workforce. "It's a prescription for disaster," says James E. Harbour, a Tro (Mich.) manufacturing consultant. "There are too many variables."

## Renschler's manufacturing, engineering



enschler certainly belies the stereotype of the buttoned-down Mercedes executive. Raised on the family farm near Stuttgart, he's as comfortable with factory workers as he is with board members. Even if he weren't 6 feet 4 inches tall, his ebullient, gregarious nature would make him stand out. His boss, Jürgen Hubbert, managing director in charge of the passenger-car unit, admits sometimes asks Renschler to don a conservative tie or jacket before addressing the board. A night owl, Renschler usually arrives at work late in the morning but toils as late as 3 a.m. As part of a plan to adapt the best operating techniques of other companies, Renschler has tapped managers from the ranks of Chrysler, Ford, Mitsubishi, and Toyota. But their varied backgrounds can spark lengthy debates. For instance, Toyotsumi Taylor, vice-president of production, spent Thanksgiving weekend of 1993 holed up in a Tuscaloosa motel with a dozen German and American col-



leagues, hashing out a factory layout. German engineers wanted a sprawling S-shaped building with departments linked by complex conveyors. But after endless wrangling—and a break for turkey dinner—those with Japanese experience prevailed, and the group settled on a compact, rectangular design.

To forge his diverse group into a team, Renschler is going all-out to erase Mercedes' stiff formality and encourage personal bonds. Hence his three-day wilder-

ness trek with eight lieutenants. Even more unusual for a top Mercedes executive, he has tried to build ties with employees at all levels. In May, he and Taylor hosted seven Alabama maintenance workers who had been sent to Germany for training. After dinner at an Italian restaurant, the group moved to a pub and then to late-night clubs, dispersing just in time for Renschler to meet his girlfriend's 10:30 a.m. flight from England. "That's the way communication gets going," he asserts, "not in an official appointment in my office."

**ADAPTABLE.** Renschler is pushing changes in Mercedes' leaden product-development process, too. To save time and money, the AAV will have 100 primary suppliers—vs. 1,000 for the just-introduced E-class sedan. In addition, suppliers get a freer hand in designing parts, sometimes adapting off-the-shelf components instead of always starting from scratch as in the past. And rather than make suppliers bid for business annually as Mercedes usually does, Renschler has been offering multiyear contracts in return for annual 5% price cuts.

Renschler has also championed in-depth market research, hoping to emulate Japanese success in tailoring products to U.S. buyers. In the past, Mercedes sought consumer input only after designs were set, but with support from Renschler and Zetsche, Folger in early 1993 organized consumer focus groups in New York, Los Angeles, Cologne, and Munich. When the S-shaped rear roof support reminded potential U.S. buyers of a homely, 1970s-era AMC Gremlin, the design was changed, perhaps averting a disaster.

Renschler's boat-rocking has won him his share of enemies within the company. "Lots of people are envious" of his rise or are threatened by the changes he's pushing, says one insider; and some are quietly hoping for him

#### PARTS TIME:

*Suppliers have been invited to be creative, too*

to fail. Such sour feelings could slow Mercedes' effort to remake itself. Top execs say the AAV project is al-

ready influencing other future products, such as the Micro Compact Car, a two-seater being developed with Swatch parent SMH Corp. A similarly freewheeling team will design it, and it will be assembled in France. But wholesale adoption of Renschler's innovations may come only if the AAV is a smash when it hits showrooms in 1997. Until then, Renschler himself is out on a ledge.

*By David Woodruff in Detroit, with Karen Lowry Miller in Stuttgart*

The power to do what  
they  
never imagined you could do

The power to do what  
you  
never imagined you could do

The power to make others  
see beyond the surface

The power to make a lifelong  
dream come true

The power to shine

The power to be accepted for  
who you really are

The power to not always  
have to ask for help

It's the power of freedom

It's the power of independence

It's the power of Macintosh

The power to be your best



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$\frac{20}{200}$

**IF**

$\frac{200 \text{ FT}}{0.1M}$

**1**

$\frac{20}{100}$

**U READ**

$\frac{100 \text{ FT}}{30.5M}$

**2**

$\frac{20}{70}$

**THIS U CAN**

$\frac{70 \text{ FT}}{21.3M}$

**3**

$\frac{20}{50}$

**GET MORE**

$\frac{50 \text{ FT}}{15.2M}$

**4**

$\frac{20}{40}$

**VALUE**

$\frac{40 \text{ FT}}{15.2M}$

**5**

$\frac{20}{30}$

**YOUR MONEY**

$\frac{30 \text{ FT}}{9.14M}$

**6**

**RE MORE**

**7**

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# GLOBAL INV

**W**hen investing in developing economies, it pays to do your homework. Just ask Josephine Jimenez.

Jimenez, co-manager of the \$1.1 billion Montgomery Emerging Markets Fund, jetted to Chiapas after Indian peasants launched an uprising in the southern Mexican state early last year. Worried that the rebellion could signify deep problems for the economy, Jimenez spent several days

poking around dusty public libraries and talking to local residents. But

it was the impassioned sermons delivered by local parish priests that convinced the Philippines-born Jimenez that big troubles were brewing in a presidential election year. "I could identify the emotional chords they were playing," she says. So as soon as Jimenez returned to her San Francisco office, "I said, 'Let's pack our bags now.'" In one swoop, she dumped nearly all the fund's Mexican holdings and moved the proceeds to Asia.

Jimenez' shift was remarkably prescient. By yearend, the pres-

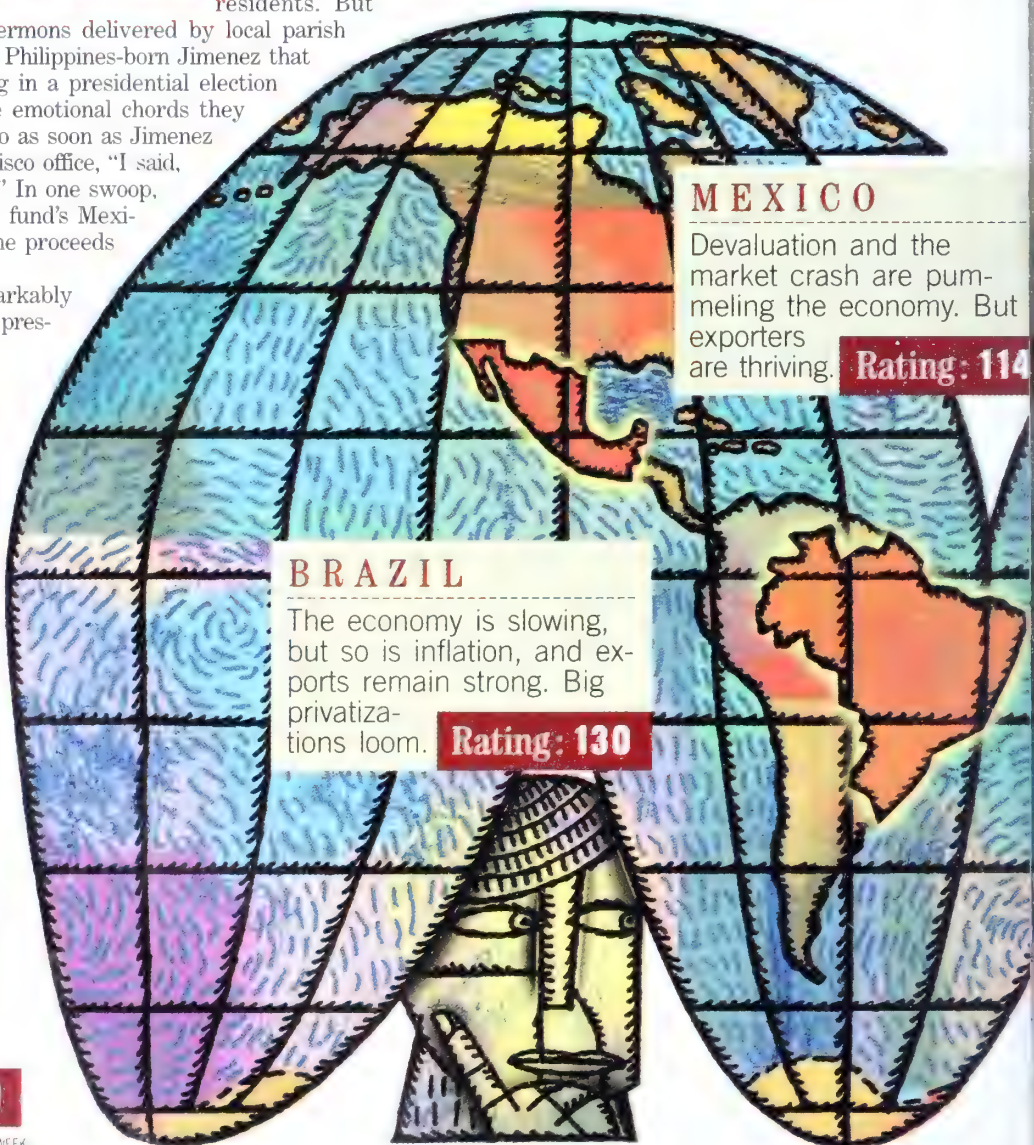
ures of U.S. interest-rate hikes and the Mexican economic and political problems that surfaced first in Chiapas had come to head. Unable to finance his country's imports with foreign cash any longer, newly elected President Ernesto Zedillo abruptly devalued the peso, sending Mexican stocks, bonds, and emerging markets around the world into a panic. Now, more than a year after her big move, Jimenez emphasizes the crucial factor in her investment strategy for emerging markets. "It's important to follow the political situation as well as companies," says Jimenez, whose fund took a hit even with her Mexico exit. "You have to pay very close attention to political risk."

## Special Report

## How They Rate

*Bankers Trust Co. fund managers have ranked leading emerging markets in terms of growth, politics, liquidity, and other factors. They view the U.S. as getting pricey. Other markets earn higher scores.*

**U.S. Rating: 100**





# STING Emerging markets hold some of the best prospects for growth

this year of the Mexican meltdown, that's advice worth listening to. Politics were largely ignored in 1993 and much of 1994, as investors seeking an alternative to rock-bottom U.S. interest rates threw cash at emerging markets with abandon, assuming that rapid economic growth would continue for years. But now that sanity has returned, the interplay between politics and economics has once again become the factor to reckon with. "We have to be more focused on stresses and strains," says Mark Breendon, manager of the New York Stock

Exchange-listed Global Privatization Fund. Indeed, Paul Durham, vice-president of Bankers Trust Co.'s Sydney (Australia)-based BT Funds Management unit, notes that "one of the lessons people learned in the past 12 months is that all emerging markets are not equal."

That maxim certainly holds true today. From Taipei to Moscow to Bogotá, there is no shortage of political jitters roiling markets. To help decide which markets to favor, BT—like many of its rivals—has developed mathematical models

## RUSSIA

Politics are scary. But the ruble has stabilized, and natural-resource stocks are cheap.

**Rating: 131**

## CHINA

Growth should revive in 1996. But money is tight. And beware of rising tensions with Taiwan.

**Rating: 95**

## ISRAEL

Booming high-tech stocks are enlivening the market. But falling rates and rising tensions.

**Rating: 143**

## PHILIPPINES

Stable politics, lower interest rates, and economic reforms are boosting the market.

**Rating: 155**

## SOUTH AFRICA

Local companies are quickly expanding across Africa. But stocks are no longer bargains.

**Rating: 119**

## SOUTH KOREA

Stocks are bouncing back as interest rates ease. And electronics exporters' profits are surging.

**Rating: 148**



that attempt to quantify the risks of investing in emerging markets. In this report, BUSINESS WEEK presents several of BT's key conclusions. Weighing the likelihood of political instability against such factors as liquidity, valuations, and expected earnings growth, Durham rates the Philippines, Indonesia, South Korea, and Israel among the top markets in the world.

In such top-rated markets, he believes, investors could reap total annual returns of 20% to 30%—much higher than they might expect in the U.S. Many of these markets have been rallying smartly in recent months (charts) as investors look to the developing world for a long-term payoff. Jimenez' fund alone has garnered some \$2 million in new cash per day this year.

Why? At a time when the U.S. stock market is near a historic high, there is still plenty of action overseas. While

it's way below its record highs, Shanghai's B-share market—the one open to

## Special Report

foreigners—has moved up 26% since May amid signs that authorities soon may loosen their anti-inflation credit squeeze. The Philippines is winning adherents for its economic about-face. The Middle East is drawing plenty of interest, too: Israel's stock market, buoyed by a takeoff in high-tech issues, is soaring. Jordan is planning privatizations and new investment and tax laws to shock the Amman Financial Market out of its torpor. And Lebanon is preparing to reopen Beirut's bourse for the first time since civil war closed its doors in 1983.

Things also seem more secure for Latin America. The Mexico City market has rebounded 51% (in dollar terms) over the past six months. Chile, whose massive domestic savings pool helped protect the Santiago market from the past months' storms, is humming along nicely. Peru is in high gear as President Alberto Fujimori presses reforms. The Buenos Aires Stock Market has soared 70% since March as more than \$4 billion in deposits have returned to local banks after President Carlos Menem's pledge to keep the Argentine peso firmly pegged to the dollar. "The tequila effect is gone from Argentina," Menem tells BUSINESS WEEK. "We have gotten over the main part of the Mexican crisis."

**HUGE CASH FLOWS.** All of this is music to the ears of many pros who have never gotten off the emerging-market bandwagon. Baring Securities International Ltd. strategist Michael J. Howell figures that investors will move some \$25 billion into developing countries' bourses in 1995, the third-largest inflow on record. Already, the International Monetary Fund estimates, 16¢ of every dollar flowing into major Western mutual, pension, and hedge funds is going to emerging markets. In 1987, two years before the Berlin Wall fell and the number of investment opportunities exploded, emerging markets gar-



## Despite dicey politics, former communist bloc nations are attracting value investors

**HUNGARIAN DRUGMAKER CHINOIN IS WINNING PLAUDITS FOR ITS STRONG R&D AND A 20% RETURN ON EQUITY**

nered barely a half-cent of every dollar fund managers raise

But 3 billion potential new consumers are now striving to enter the global economy. That's opening up investment in such critical industries as telecommunications, banking, construction, and consumer goods, where demand has been repressed for decades. "The bottom line is that emerging-market economic development is happening on a titanic scale," says Arnab Bhattacharya, chief investment officer for London's Foreign & Colonial

Emerging Markets Ltd. "Mexico was just a hiccup. If you're really taking a five-year view, nothing has changed."

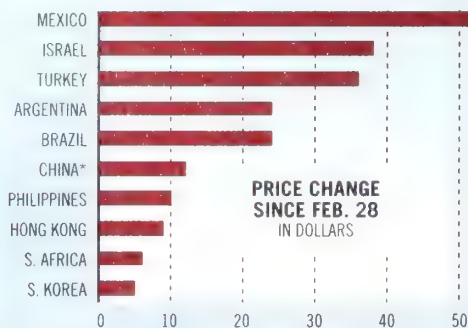
Since many markets and mutual funds have yet to fully recover the losses, that may be overstating things. And the "hiccup" was in fact an important warning to investors and government officials that they will have to factor into their calculations a powerful new force in global investing: so-called hot money—huge pools of institutional capital that can be moved in and out of economies with lightning speed.

To be sure, as the IMF recently concluded, Mexico's financial crisis was sparked as much by disillusion

## Emerging Stock Markets Are Recovering



DATA: BARING SECURITIES INTERNATIONAL LTD., BLOOMBERG FINANCIAL MARKETS



\*SHANGHAI "B" SHARE INDEX





domestic investors as by offshore money managers leaving town. Nevertheless, once the big-bucks foreigners joined the locals' stampede, there was little to stop the run on the markets. "The rules of the game have really changed," says Jorge Suárez-Vélez, managing director of Mexico's Afin Securities. When hot money flees, even a country such as Mexico, with a North American trade deal, a tight national budget, and single-digit inflation "can still get into trouble with the foreign funds."

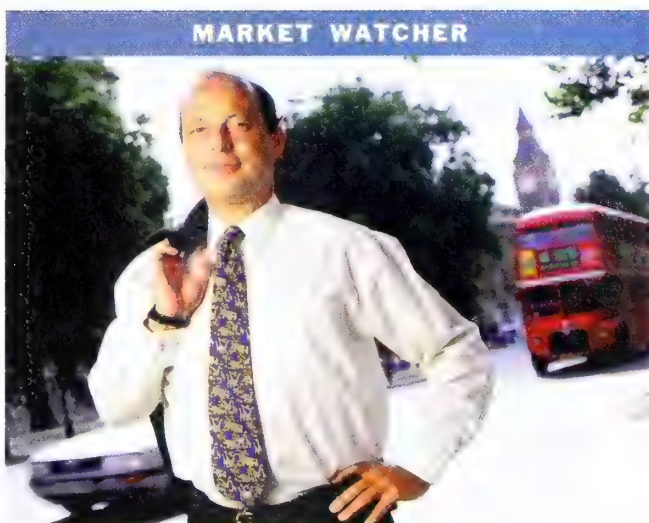
That realization is having a potent disciplinary effect across the developing world. In country after country, government officials and central bankers are scrambling to find ways to boost savings, promote direct foreign investment, and stabilize their currencies as ways

reducing dependence on volatile portfolio flows. They're also improving government and corporate disclosure to make investors feel more at home. As part of the price of its \$50 billion bailout from the U.S. and other industrial nations, Mexico is now making regular announcements about the level of its hard-currency reserves. Notes Buenos Aires Stock Exchange President Julio Macchi: "The way to cushion the effect of outside forces is to release as much information as possible about macroeconomic policy and companies."

**FACE TALKS.** This change in attitudes will go a long way toward validating the fundamental case for investing in emerging markets. Simply put, for all their fits and starts, emerging markets still hold some of the world's best prospects for robust economic growth and healthy earnings. In a year when the U.S. domestic product of the U.S. and Western Europe may expand by little more than 2% and Japan is battling recession, Asian output, for instance, is expected to grow by a solid 7.6% in 1995, according to the Union Bank of Switzerland. The Middle East, benefiting from Arab-Israeli peace, could grow by more than 4%. Even Mexico, which is likely to see its economy shrink a staggering 5% this year, is likely expected to be moving forward by 1996 or so. All told, the IMF believes developing countries will grow twice as rapidly as the industrial world for the remainder of the decade. Despite the growth story, stocks in many

**Worries over tensions with China have pushed Taiwan's stocks down nearly 40%**

**REST IN TAIPEI: BEIJING HAS BEEN TALKING ONLY OF LAUNCHING AN INVASION**



## Mark Breedon

*Manager, Global Privatization Fund*

**WHERE TO INVEST** Start with South African steel and Indonesian and South Korean telecoms. Then go for utilities in Hungary.

**WHAT TO AVOID** Shun commodities. Watch out for disappointing growth in Latin America, especially in Mexico.

emerging markets still can be cheap. Take Teléfonos de México, the phone utility that many view as a bellwether for emerging-market stocks worldwide. With its American depositary receipts (ADRs) trading around \$32, Telmex is now 56% off its record high of 1994 and is trading near where it was when the privatized company was floated on the NYSE in 1991. But since then, Telmex has poured nearly \$10 billion into everything from rural phones to digital networks of fiber-optic cables. At today's stock price, you get all that investment for free.

The value gap is also apparent in the former communist bloc. Chinoin, a Hungarian pharmaceutical maker partly owned by French drug manufacturer Sanofi, has won plaudits for its strong research and development efforts and its 20% return on equity for the past three years. Yet its stock fetches a price-earnings ratio of less than 4. Surprisingly enough, however, it's





Russia that is making some brave value investors take notice. Tumultuous politics, tottering banks, stumbling economy, and questionable corporate reporting faze all but the most intrepid investors. But Moscow's stock market is sending out deeper and deeper roots. A few privatized corporations even are working on issuing ADRs.

Many fund managers are high on Lukoil, the Russian energy giant whose shares trade in Moscow. Although it's one of

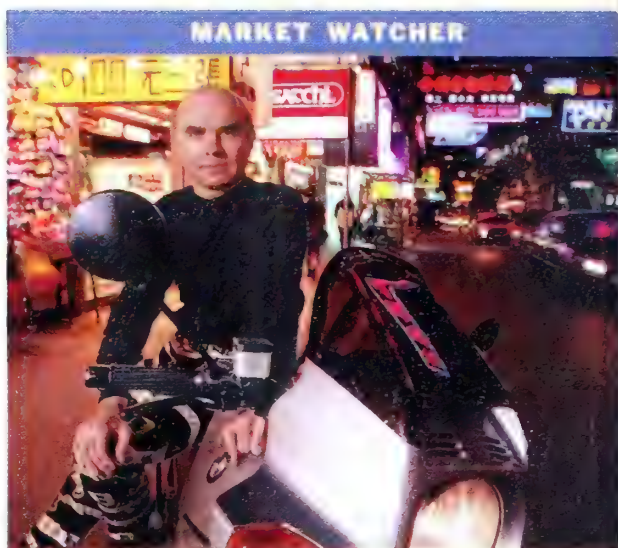
the world's largest petroleum producers, controlling 15% of Russia's oil output, investors value Lukoil's reserves at a tenth of what they're willing to pay for those of Exxon Corp. But will such a gaping disparity persist? Atlantic Richfield Co., betting it won't, is spending \$250 million on bonds convertible into Lukoil stock. Says Franklin Templeton emerging-market guru Mark Mobius, who recently launched a \$70 million Russian closed-end fund in the U.S.: "Change is embedded in the psychology of the people."

**WILD TIMES.** While country funds such as Mobius' Russian vehicle appeal to many investors who want to take a direct stake in a single economy or company, many market pros suggest that a much safer approach is via emerging-market mutual funds that invest their assets around the world (table). That's because individual markets can be frighteningly illiquid and, as a result, often gyrate wildly. "I wouldn't want to concentrate on any one country or region," says Alliance Capital Management global analyst Robert G. Heisterberg, who helps manage some \$2 billion in emerging-market assets spread among two dozen countries. "In a lot of markets, it's feast or really get hurt."

Choosing cheap investments, either funds or individual securities, won't necessarily insulate investors if politics go awry. Mexican President Zedillo is facing a 10.5% drop in GDP during the second quarter and a painful credit squeeze on the country's middle class. To defuse a political challenge from a restive debtors' movement, he is channeling more than \$1 billion into a plan to slash interest rates for consumers and business. Investors fear that if he spends too freely, the peso will weaken again, erasing gains from the recent rally in stocks.

Politics are even dicier in Colombia. Bogotá's stock market has fallen more than 10% over the past month as President Ernesto Samper declared a state of emergency amid allegations that his election campaign received up to \$6 million from the Cali drug cartel last year. But Baring Securities' Bogotá research chief, Guillermo Serrano, thinks Colombia's democracy and markets are durable enough to weather the crisis without too much more damage if Samper should resign.

Some analysts are more concerned about the likelihood of po-



## Marc Faber

*Independent Hong Kong money manager*

**WHERE TO INVEST** Go for ultra high-risk markets where big gains are possible. That means Russian oil and gas stocks and North Korean debt.

**WHAT TO AVOID** Steer clear of other developing markets unless U.S. stocks rally further. Be especially wary of political tensions in Asia.

litical strife in Asia, up to now an oasis of comparative calm and torrid growth. Just last year, analysts and funds were promoting India as the new gold mine for investors. More recently they were boosting Taiwan, saying that earnings were soaring and the market looked sure to climb. But Taiwan's stock market has plummeted nearly 40% this summer as China has stepped up pressure on President Lee Teng-hui by testing ballistic missiles scarcely 100 miles offshore and talking openly of an invasion. India, too, has become a question mark. A religious party coalition in the key state of Maharashtra is frightening away foreigners by canceling a \$2.8 billion power-plants deal with Enron Corp. Developments such as these prompt analyst Alan Stoga of the consulting firm of Kissinger Associates Inc. to conclude that the potential for further instability looms over the entire region.

With the cold war over, China, Japan, India, Indonesia and possibly Russia will be competing for influence in the

## A TOUGH YEAR FOR FUNDS

## Largest U.S.-listed emerging-market funds

### OPEN-END FUNDS

|                                 | ASSETS<br>BILLIONS | 1995 TOTAL<br>RETURN* |
|---------------------------------|--------------------|-----------------------|
| TEMPLETON DEVELOPING MKTS. I    | 2.2                | 4.2%                  |
| FIDELITY EMERGING MKTS.         | 1.4                | 0.2                   |
| MERRILL LYNCH DEV. CAP. MKTS. A | 0.4                | -3.1                  |
| MONTGOMERY EMERGING MKTS.       | 1.1                | -3.4                  |
| MORGAN STANLEY INS. EM. MKTS.   | 1.0                | -6.2                  |

### CLOSED-END FUNDS

|                              | ASSETS<br>BILLIONS | 1995 TOTAL<br>RETURN* |
|------------------------------|--------------------|-----------------------|
| CHILE FUND                   | 0.4                | 9.5%                  |
| G.T. GLOBAL DEVELOPING MKTS. | 0.4                | -2.6                  |
| MORGAN STANLEY INDIA         | 0.4                | -3.3                  |
| KOREA FUND                   | 0.6                | -4.1                  |
| MORGAN STANLEY ASIA-PACIFIC  | 0.7                | -8.0                  |

DATA: MORNINGSTAR INC.

\*Through Aug. 2



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"Incredible levels of profitability are possible" in Brazil, one analyst says

TELECOM COMPANIES SUCH AS TELEBRAS AND TELES P ARE PULLING IN A LOT OF CAPITAL

cific. Moreover, most of the region's major countries face leadership changes in the next five years. That's certainly a point to consider in China, where the question of who will run the country after the death of the ailing Deng Xiaoping is a major concern. As a result, Stoga advises investors to look for "much higher returns than they seem willing to accept in Asia. The risk in the region is going to be higher, not lower."

**ACHING HEADS.** Others counter that they are factoring in the risks. The trick, they say, is to insist on high enough potential profits to compensate for the possibility that your holdings will be wiped out. "To invest in an emerging economy and have all the headaches that go with it, I should see substantial capital gain potential," says independent money manager Marc Faber. "Otherwise, it's hardly worth it."

To Faber, that means taking a flyer on oil and gas stocks in Russia. "If Russia can move successfully to be a Western capitalist society," he predicts, "its shares could be mind-boggling." But other Asian pros prefer sticking closer to home. Hong Kong-based analyst Alan Butler-Henderson of Baring Securities recommends moving into the British colony despite its imminent takeover by Beijing in 1997. He argues that Hong Kong's trade balance is improving as the economy slows. That will boost market liquidity, attract foreign investors, and push the Hang Seng Index, already up 12% this year, past the record high of 12,157 it set in 1994. Fund manager Mobius is so convinced that the colony will remain the gateway to the mainland's economy that he has plunged most of a \$4 billion wager on China into companies based in Hong Kong. Says Mobius: "We're betting life will go on."

Other Asia hands are looking to South Korea, where declining interest rates, cooling

inflation, and rapid earnings growth are giving equities a lift. Schroder Capital Management International Inc. Director Laura E. Luckyn-Malone is putting her faith in Samsung Group. Its semiconductor sales are surging, yet it trades at a modest price-earnings ratio of 8. "Samsung is really giving the Japanese a run for their money," she says. "They're going from strength to strength."

While Asia remains the world's growth machine, some pros believe South Africa has equal potential. Emerging from years of apartheid and worldwide opprobrium, heavily industrialized South Africa is vying to become the commercial hub of the vast area south of the Sahara. There are drawbacks: soaring crime and the nation's future after President Nelson Mandela, who at 77, has taken on legendary proportions. But that doesn't stop Carmen Maynard, director of fund management at Johannesburg's Martin & Co., from recommending such mainstays as

has been high, Mexico's trade balance is in the black, the p appears stable, and the solvency crisis that triggered the p down has evaporated in the face of U.S. aid. Most of the g ernment's *tesobonos*—dollar-linked debt that came back haunt Mexican and foreign investors alike—have been p off. And the government has returned to international cap markets, selling \$2.1 billion in debt this summer.

Amid the rebuilding effort, analysts are starting to find ue in Mexican stocks again. Many like Penoles, a big silver-n ing group that has benefited from rising bullion prices and

export boom. Recent analysts have add Desc, a conglomer with holdings in pet chemicals and a parts, as well as E presas La Moderna cigarette producer t has moved into fr vegetable exports a acquired Asgrow S Co. Grupo Carso, big holding compa that owns a chunk Telmex, also rema popular for its ha nosed skill at handl its finances.

Brazil and Argent offer similar valu Malcolm Gibson, an a lyst at Roberts Cap Markets in Bue Aires, thinks Argent steelmaker Siderca fers "tremendous c flow," rising expo and annual earni growth of 35%. A Pérez Companc, the energy group, is p anding across the b der. Its recent purch of the Brazilian elec company Escelsa co bring "massive prod tivity gains."

Some Brazilian inv tors are taking he

#### MARKET WATCHER



**Laura E. Luckyn-Malone**

Manager,  
Schroeder Asian Growth and  
Emerging Market funds

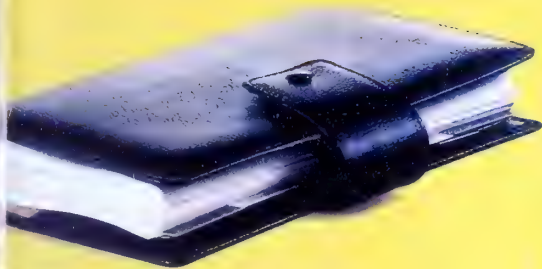
**WHERE TO INVEST** Focus on Thai and Malaysian bank and homebuilding stocks, Korean high-tech shares, and Brazilian telecom issues.

**WHAT TO AVOID** Taiwan looks cheap but "it's a casino-type market where it's very difficult to be successful."

## Special Report



1992



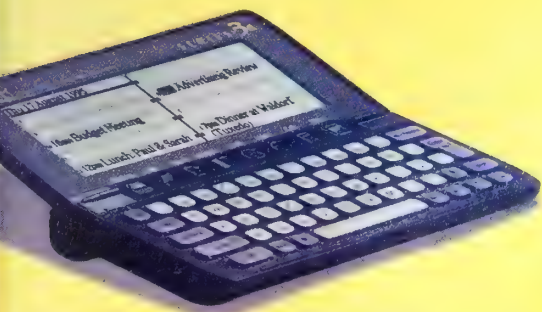
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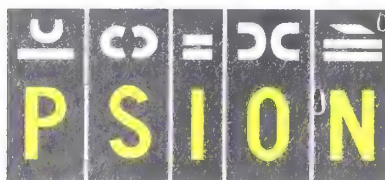
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from President Fernando Henrique Cardoso's efforts to turn the economy away from consumption and toward privatizations and investment-led growth. Ulysses Vasconcellos Diniz, director of global sales and distribution at São Paulo's Unibanco,

## Special Report

thinks telecommunications will benefit most from this switch. With a Baby Bell-style industry restructuring likely, he is betting on Telebrás, the AT&T of Brazil, and Telesp, the São Paulo local phone provider, as big winners. Others are focusing on state-controlled Companhia Vale do Rio Doce, the world's biggest iron ore producer, which Cardoso wants to sell off for \$9 billion next year. Raves Alliance Capital's Heisterberg: "The Brazilians have survived inflation of 5,000%. The quality of their business management is outstanding. Incredible levels of profitability are possible."

Although such euphoric forecasts have become increasingly common, no one will fault you if you gaze upon them with a gimlet eye. What the past few years have taught many investors is that in emerging markets, hot money can cover a multitude of shortcomings. As emerging markets come out from under the shadow of Mexico, it would be wise to consider a few key points before you take the leap. How stable are politics in the country and the region? How well are policymakers managing currencies and economies? Despite the markets' setback, maintains fund manager Breedon, "over time, you'll get better returns in the emerging markets." The question, as always, is whether you're willing to take on the risk.

*By William Glasgall in New York, with Dave Lindorff in Hong Kong, Drusilla Menaker in Johannesburg, Ian Katz in São Paulo, Elisabeth Malkin in Mexico City, and J. Javetski in Paris*

# THIS ARGENTINE GIANT WANTS A LITTLE RESPECT

**B**ehind the wheel of his Ford Galaxy, Luis Angel Castillo weaves through the maze of the Luján de Cuyo refinery in the Andean foothills of western Argentina. Just a few years ago, Castillo, manager of the refinery, would have encountered scores of maintenance workers during his rounds. Today, the facility seems all but deserted. The staff has been slashed from 700 in 1990, when it was state-owned, to just 49, now that its operator, YPF, is in private hands. "If everything is going well, the place runs itself from the control room," he boasts. "The fewer people, the better."

Efficiency is the mantra of YPF these days. Attempting to transform itself from elephant to gazelle, YPF, which controls half of Argentina's oil market, has cut its workforce to 6,750 from 51,000. Once aloof and arrogant, it is now the most public-relations-conscious company in the country. Its logo beams down from shiny new outlets selling only environment-friendly unleaded gasoline. And it's making money. Deficit-ridden throughout the 1980s, YPF netted \$401 million in the first half of 1995, two years after it went private. Yet it is still looking for respect where it craves it most: on the floor of the New York Stock Exchange.

Although Americans and other overseas investors now own half of YPF's stock, its shares have languished since its \$3 billion initial public offering in 1993. With YPF

American depository receipts now around \$18, Merrill Lynch & Co. First Vice-President Constantine D. Fliakos figures the company is trading at half of the value of its net assets. Its oil and gas reserves alone—1 billion barrels of crude and 8.5 trillion cubic feet of gas—may be worth \$29 per ADR. "This is one of the cheapest integrated oil companies in the world," says portfolio manager James A. Shore of San Diego-based

tion, initiated a month before before Estenssoro's death, was particularly unsettling to investors. Many had bought YPF as a pure play on Argentina and were unhappy with the oil company going global. Their criticism has stung YPF and illustrated the inexperience many emerging-market corporations have in massaging new foreign stockholders. "We weren't expecting that kind of emotional reaction," admits new CEO Nells León,



**DEFICIT-RIDDEN THROUGHOUT THE 1980s, YPF NETTED \$401 MILLION IN THE FIRST HALF OF 1995**

68, who was a close associate of Estenssoro. "They're not used to an emerging-market company buying a U.S. company."

León insists he's continuing Estenssoro's plans. He's counting on Maxus' offshore technology, honed at its big Indonesian oil-producing operations, to give YPF a leg up on exploring Argentina's coastline. With domestic oil output expected to rise 15% this year, to 394,000 barrels a day, León also wants to sell 1 billion cubic feet of gas a day to Brazil and more to Chile. And he's stepping up exploration in Bolivia, Ecuador, Chile, Peru, and the Gulf of Mexico. He's not the showman his predecessor was, but León is just as determined to put YPF on the roster of major oil producers—while finally giving shareholders something to smile about.

*By Ian Katz in Luján de Cuyo, with bureau reports*

Brandes Investment Partners Inc., which has snapped up 3.5 million YPF shares.

**UNSETTLING.** Why so cheap? Start with jitters over Latin markets and the economic squeeze Argentina has been forced to endure since the Mexican market collapse earlier this year. Weighing the stock down even more heavily are YPF's controversial purchase of Maxus Energy Corp., a Texas oil and gas producer burdened with \$1.1 billion in debt, and the death in a plane crash last May of YPF's dynamic CEO, José A. Estenssoro.

The \$800 million Maxus acquisi-

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BY GENE G. MARCIAL

## MCI: SET FOR MORE OVERSEAS CALLS

In 1993, when the Dow was up to 3600 and investors were flocking overseas, investment manager Wayne Nordberg kept on buying American. His faith in the Dow has paid off. But in spite of the market's sharp runup, value-player Nordberg has remained bullish.



**NORDBERG HUNTS FOR LAGGARDS**

He is, in particular, snapping up stocks whose price-earnings ratios have lagged behind the Dow's and whose worth remains unrecognized. One such stock: MCI Communications (MCIC).

The second-largest U.S. long-distance carrier, MCI "is destined to become a global giant in telecommunications, yet the Street is unimpressed," notes Nordberg, partner and head of equity investments at Lord, Abnett & Co., which manages some \$18 billion.

MCI's stock has hovered between 20 and 24 all year. Given its 15%-to-20%

shortly, similar to its deals with British Telecom and News Corp.

Last September, MCI signed an accord for British Telecom to invest \$4.3 billion for a 20% voting stake in MCI. The two companies formed a joint venture to provide communications services to multinational companies. And in May, MCI agreed to invest up to \$2 billion in News Corp. to create and distribute information and entertainment worldwide.

The Street has frowned on these alliances, partly out of concern over a dilution in MCI's earnings. "But it is exactly that strategy of alliances that will make MCI a leader in global long-distance communications," says Nordberg. Links with British Telecom and News Corp., he explains, give MCI access to Europe and Asia. The News Corp. deal, says Nordberg, will make MCI a player in entertainment software for distribution through satellites and wireless networks.

## DESIGNS ON THIS GIZMO MAKER

Stratasy's (SSYS) has a strange name. And it's odd in another way: It wasn't a hot stock when it went public in October, at 5 a share, but this year it has been a scorcher, climbing from 6 in early June to 14½ on Aug. 29. The company lost \$1.1 million in 1994, on sales of \$3.8 million. So what's going on?

Analysts are projecting big numbers: They claim 1995 sales will jump to \$9 million, with earnings of \$164,000, or 7¢ a share. Next year, projections are even rosier: sales of \$24 million and earnings of \$2.3 million, or 74¢. Pie in the sky? Not so, says analyst John Duffy of Brookhill Equities, who predicts the stock will hit the low 30s in two years.

Stratasy's is in "rapid prototyping." It makes gizmos that let engineers create models out of plastic, working directly from computer designs, in a matter of hours. In many industries, prototypes are still produced by hand-sculpting or machining that takes weeks.

With such advanced technology, "the likes of General Electric, Dow Chemical, or Union Carbide would like to acquire Stratasy's while it's cheap," says one investor. "It's a high-margin business."

One big holder, with 13.7%, is IBM. The stake stemmed from Stratasy's purchase in January of IBM's prototyping technology. The deal merged IBM's technology with Stratasy's system.

Joe Salvani, president of Salvani Investments, has acquired 3% of Stratasy's

and says it's one of the few companies that applies its own technology toward making an end-product. He says the company is working with Ford Motor for a device big enough to make actual-size prototypes of cars.

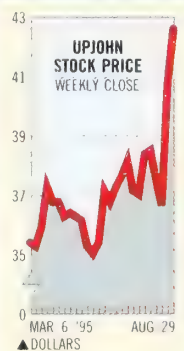
## WILL P&G UPSET UPJOHN'S MATCH?

Perennial takeover target Upjohn (UJ) finally found a fiancé—Sweden's Pharmacia—after more than a year of rumors. But don't be too sure this wedding will come off without a hitch.

Speculation about a third-party bid may prove to be true. So say some takeover pros, who claim that none other than Procter & Gamble will go after the drugmaker—at a price above Upjohn's current 42. Whispers are that P&G will offer at least 50 a share.

The proposed \$6 billion Pharmacia-Upjohn stock-swap merger was based

### NOT QUITE READY FOR THE ALTAR



DATA: BLOOMBERG FINANCIAL MARKETS

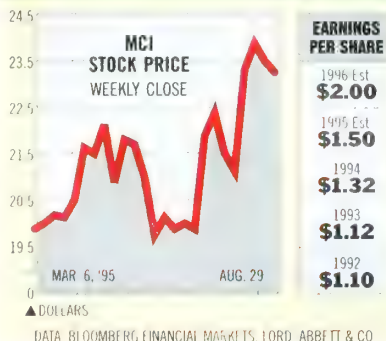
on an Upjohn price of 37½. Since the Aug. 20 announcement, Upjohn's stock has been on the rise, indicating that another bidder may have come in. P&G acknowledged that it is striving to be a world leader in prescription and over-the-counter drugs... "and we are looking for opportunities

the business," including acquisitions. A Upjohn spokesman wouldn't comment on whether it has received another offer. One investment banker insists that Upjohn, having announced that it's ready for sale, can't reject an offer higher than the Pharmacia bid.

P&G's long-term plan is to expand its pharmaceutical business. It has often told analysts, says one big P&G investor, that it is committed to becoming a world player in health care. Widely known for household cleaning products, P&G also makes and distributes in 60 countries personal-care products, including prescription and over-the-counter remedies.

Upjohn would bring to P&G's medicine chest such products as Xanax for anxiety, Micronase for diabetes, Halcion for sleep disorders, Rogaine for hair loss, and Motrin as an anti-inflammatory.

### GLOBAL HOOKUPS AHEAD



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| 1995 Est | \$1.50 |
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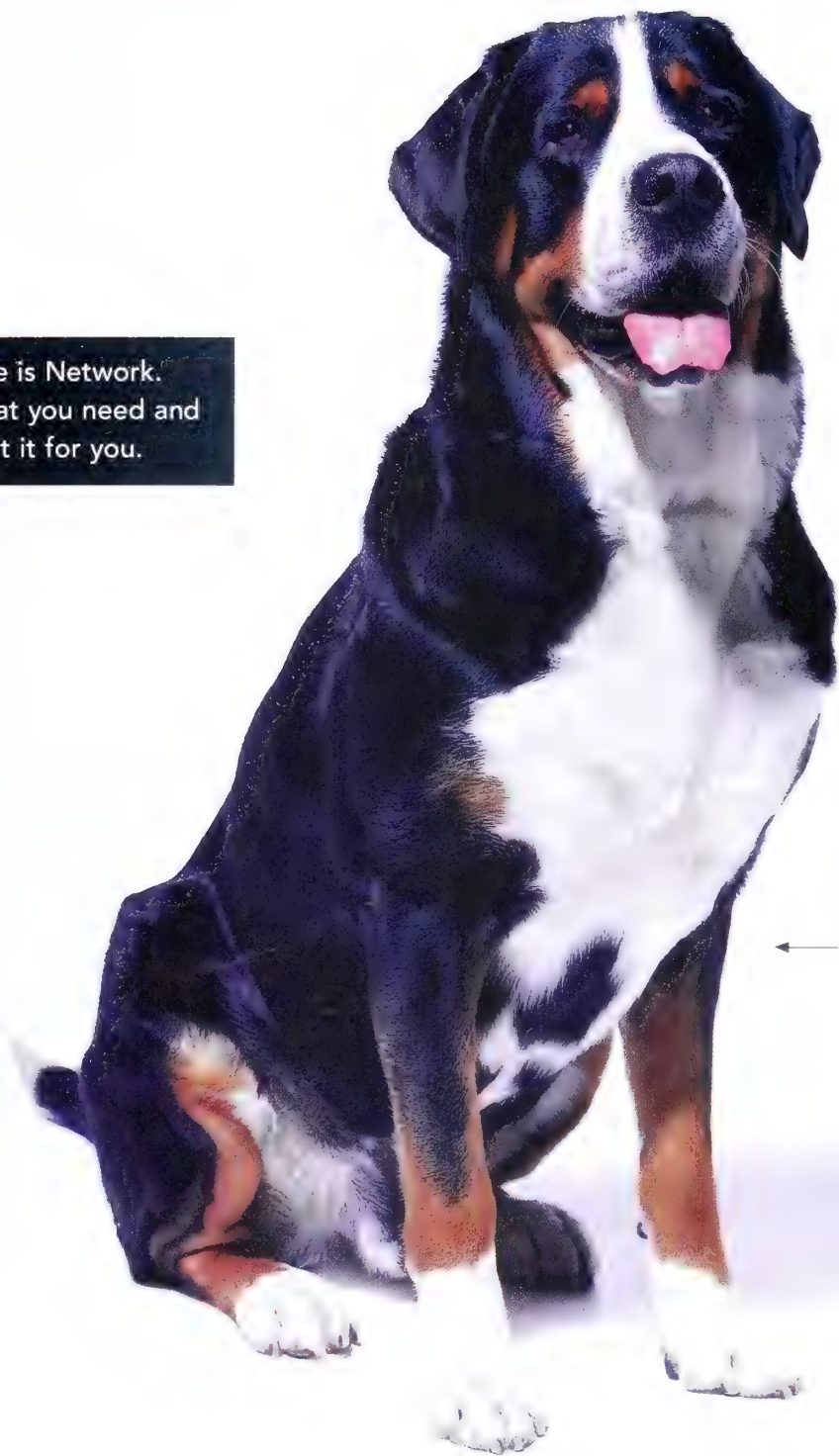
DATA: BLOOMBERG FINANCIAL MARKETS, LORD, ABBETT & CO

yearly earnings growth and big goals for global expansion, Nordberg figures it will hit 40 in two years.

Many think a shakeout is overdue in telecommunications and that cash-laden MCI, with revenues of \$13.3 billion last year, will either merge with or acquire another long-distance outfit or an information-entertainment company.

Nordberg doesn't discount such a prospect. He believes that MCI will first strike an additional strategic alliance

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# WHO NEEDS THE I-WAY ANYWAY?

GTE thinks core phone services are the best route for now

**C**huck Lee certainly knows a lot about corporate turmoil. Growing up in Pennsylvania farm country, the young man who would become chairman and chief executive of GTE Corp. first set his mind on running U.S. Steel. He joined the company fresh out of Harvard business school—just in time to experience the slow demise of the American steel industry. In 1971, he moved to Penn Central Corp.—only four months before the bankruptcy of that high-flying conglomerate. Next stop: In 1980, Lee became chief financial officer at Columbia Pictures, where he was hired to tighten financial controls in the wake of a check-forgery scandal.

So Lee might be excused a bit of caution as he ponders the seismic shifts rocking the telecommunications industry. With a résumé heavy on corporate cleanups, it's no surprise that Lee, head of \$20 billion GTE, the world's No. 4 telephone company, is moving with far less haste than such rivals as Bell Atlantic Corp. and Pacific Telesis Group. While others race to stake out a spot on the Information Superhighway as entertainment, cable, and telecommunications converge, the 55-year-old Lee prefers to concentrate on improving GTE's core phone franchise.

So for GTE, there have been no splashy announcements of cross-industry mergers. No signings of Hollywood media maven. No radical new technologies. Instead, Lee is leading a \$1.3 billion restructuring of GTE's local phone unit—the source of 80% of revenues—while cutting \$1 billion in operating costs. “We don’t blow smoke,” he says. “We haven’t chased a pot of gold at the end of the rainbow.”

Think of it as a “bird-in-the-hand” strategy. While high-profile plans for cable industry alliances, online video, and other I-way services may take years to bear fruit, Lee sees big growth in phone services. “What amazes me is how people don’t appreciate what a great business we are in,” he says. For now, there’s plenty to appreciate: For the first half of

1995, operating income rose 7%, to \$2.5 billion, on a 4% rise in revenues, as cost-cutting offset pricing pressure.

**IN FLUX.** The question is whether GTE’s go-slow strategy will work long term, as deregulation opens the market. Like the Baby Bells, GTE—which provides local service to 20 million people in 28 states—will face new rivals, from cable companies such as Time Warner Inc. to long-distance suppliers such as AT&T. And emerging technologies such as the Internet threaten everyone. “The market is in flux,”

says Sanjay Mewada, an analyst with the Yankee Group Inc., a Boston-based technology consultancy. “The race has really started.”

GTE can’t rest on its laurels in the phone business. Lee and newly appointed President Kent B. Foster have plenty to do to improve operations and make GTE quicker on its feet. It has long lagged behind Baby Bell rivals in profitability and efficiency. Although GTE’s margins are much improved since Lee was named CEO in 1992, employee productivity still runs below industry averages. So in June, Lee shook up management, making longtime phone chief Foster his apparent heir apparent and placing him in charge of combining GTE’s traditional and wireless units.

GTE is also in the midst of axing roughly 17,000 employees, or 20%, from its telephone workforce. And it has slashed more than 200 service centers, using technology to do the work people once did, while spending close to \$4 billion a year upgrading its networks to handle more digital and video transmission.

Still, GTE must overcome a history



## How Chuck Lee Is Reshaping GTE

### RESTRUCTURING

Spending \$1.3 billion on reengineering moves that will slash 17,000 jobs, replace people with technology, and speed business practices. Lee’s goal: Cut annual operating costs \$1 billion by 1997.

### TECHNOLOGY

Betting heavily on PCS, a cheaper alternative to cellular. Meanwhile, taking a cautious approach to the Information Superhighway: Building a video network and joining a consortium with Disney and three Baby Bells.

### INTERNATIONAL

Lee wants to double GTE’s global presence, which now accounts for 13% of sales and 12% of profits. Already a big player in Venezuela and Argentina, GTE is eyeing Indonesia, China, and other markets in Latin America.

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**Canon**



poor customer service that dates back to the 1980s. In Santa Monica, Calif., service was so bad that officials tried to remove GTE as the local phone company. "We were the pits," Lee admits. He claims big improvements—GTE has largely done away with its old system of taking customer service requests, which required writing up a problem and passing it along for resolution. Now, using personal communication services and specially designed software, service reps can solve 70% of all problems on the initial call—double the mid-1980s success rate. Repair workers, meanwhile, plan their schedules on laptops, cutting down time and speeding responses.

**VULNERABLE?** But with rivals on the way, more than good service is needed. In California—where local toll calls are opening to competition—GTE is offering steep discounts. Jim Cawthorn, Los Angeles-based regional telecommunications manager for Allstate Corp., saw GTE's rates fall from 12.5¢ a minute to 5.5¢ when he signed up for a year's commitment. GTE's Foster says that in the highly competitive L.A. suburbs, it has lost only 10% of its market to Pacific Bell and others. Foster counts on getting that back once GTE can offer long-distance service, possibly by January.

Still, competitors lurk. MFS Communications, a small but fast-growing provider of corporate phone services, is already cherry-picking GTE customers around Tampa and Dallas suburbs with its state-of-the-art fiber-optic networks. Time Warner is testing telephone service in Rochester, N.Y. By 1997, it's likely to attack some of GTE's more lucrative phone franchises, including Hawaii, where it says poor service makes GTE vulnerable. "It is not unreasonable to expect to grab 15% market share within several years," says Time Warner phone chief Tom Morrow. But Lee notes the cable companies' own rep for lousy service. "We'll hold our own," he says.

Lee knows he needs to counterpunch with new businesses. So far, GTE has barely tested the Information Superhighway: Main Street, an early interactive experiment aimed at providing home banking, games, and other entertainment services over phone lines, has had little success. So now GTE is spending \$250 million to build its own video network to be delivered over cable; it expects to have 500,000 homes by early 1996. And GTE has joined a \$500 million programming consortium with Walt Disney Co. and three Baby Bells, though the venture is still in its infancy.

Meanwhile, the bulk of GTE's investment is going toward expanding its

telephone franchise. The company has spent heavily to build a national cellular business; revenues—at \$1.6 billion—are growing at close to 50% a year. And last year, GTE launched the first residential PCS service, a cheap alternative to cellular. With 150,000 customers so far, GTE is now licensing its service to others.

Pushing forward on the international front, GTE is taking ownership stakes in the phone networks of Venezuela, the Dominican Republic, and British Columbia. It won the Argentine cellular franchise in 1994 and is prospecting in Mexi-

co, Indonesia, and China. International services provide about 12% of GTE's earnings and 13% of sales—figures the company plans to double over five years. But overseas markets haven't always paid in the short term: Disputes with the Venezuelan government have led to severe foreign exchange problems and heavy losses for GTE's local unit. But Lee argues that the long-term potential is huge, and sides, with the competitive turmoil in starting to roil U.S. phone markets, that developing-world plays may not seem risky after all.

By Tim Smart in Stamford, Conn.

## STRATEGIES

# DON'T STEP ON MY BLUE SUEDE HUSH PUPPIES

A '50s classic revamps in day-glo colors—and it's a '90s smash

The trendy Pleasure Swell boutique in Los Angeles is in a frenzy, thanks to the latest fashion fetish gripping Hollywood's famous feet—Hush Puppies. If Sharon Stone comes to pick up another pair, she'll have to take a number. "I can't get my waiting list under 100 people," moans 28-year-old owner Joel Fitzpatrick. "Kitsch Americana is in."

Hush Puppies? Those fuzzy, fuddy-duddy suede shoes last in vogue during the Eisenhower Administration? Yep, they're back—this time around, tarted up in shades of green, purple, and pink. And that has made Hush Puppies' conservative parent, Wolverine World Wide Inc., a hot ticket on fashion runways and on Wall Street. With analysts predicting net income will leap 25% this year, to a record \$21 million, on sales of \$415 million, the stock is trading at nearly double its 52-week low of 13½ in December. "It's like an angel came down from heaven and blessed this company," says analyst David Jar-

rett of Gerard Klauer Mattison & Co.

A combination of spruced-up styles, stringent restructuring—and plain luck—has clearly put Wolverine cloud nine. The retro craze has finally given Hush Puppies some cachet. This fall, for the first time ever, fashionable

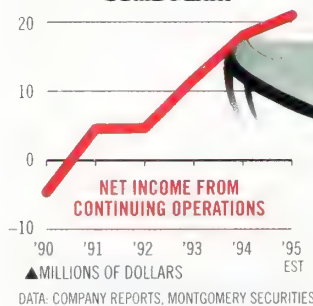
department stores such as Macy's and Bloomingdale's will be stocking the \$70 shoes. And Wolverine is adding a third shift at its Rockford, Mich., factory to try to catch up with demand. Even Wolverine Chief Executive Geoffrey B. Bloom, 12-year-old daughter Jessica, is on a waiting list for a pair of pink puppies. "I promised to get her a pair for back to school," Bloom says.

Hush Puppies' sudden fame comes after years of fruitless efforts to reach younger buyers. The company developed generic leather pumps and wing tips, with advertising aimed at baby boomers, while pushing Grandpa's blue suede lace-up "Duke" and slip-on "Earls" o-

## HOT DOGS SNAZZY HUSH PUPPIES BOOST WOLVERINE'S SALES...



## ...AND GIVE PROFITS SOME FLAIR



DATA: COMPANY REPORTS, MONTGOMERY SECURITIES

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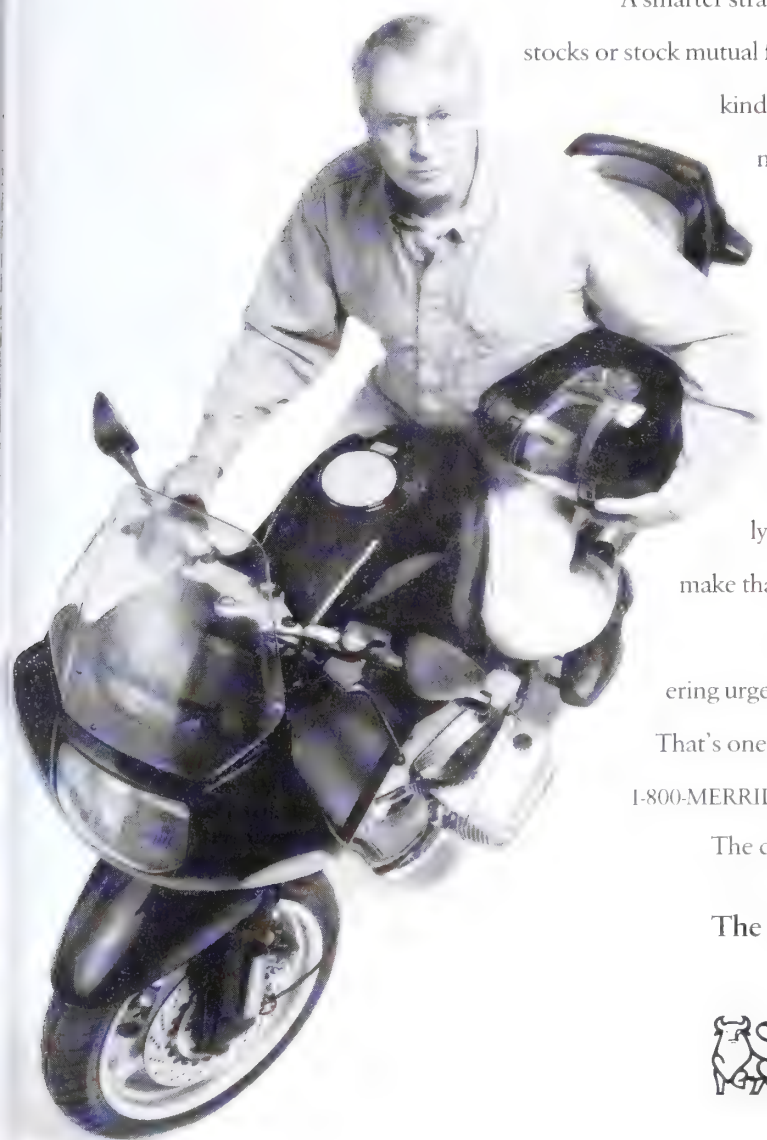
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# The Corporation

the back of the closet. "We spent \$10 million in advertising to try to convince people that we no longer made those old Hush Puppies," Bloom says.

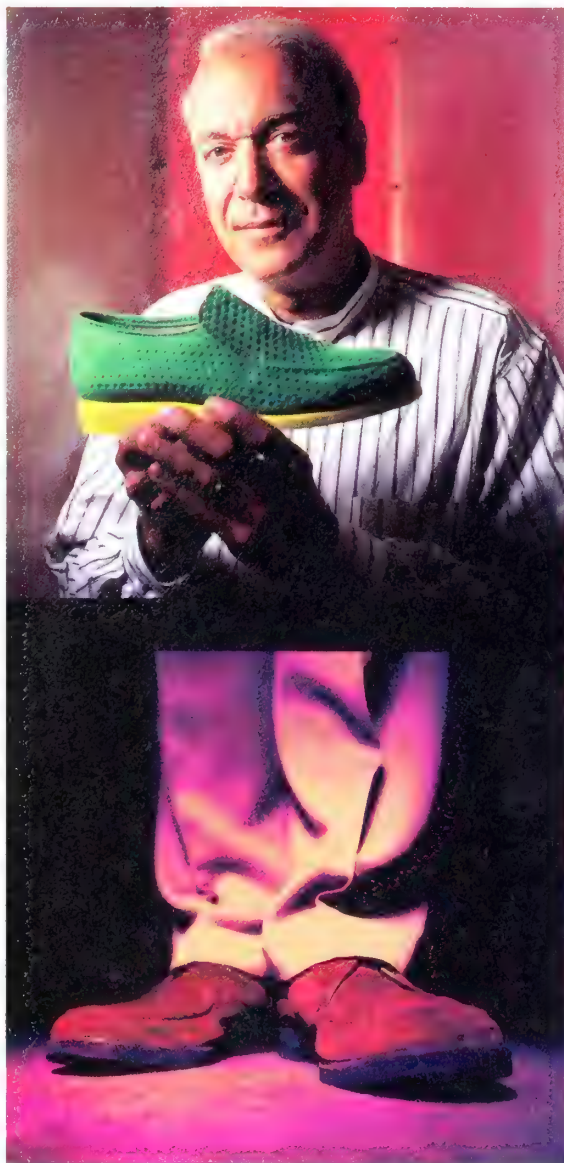
Then Tom Hanks brushed up those old Hush Puppies by wearing a pair in the final, tearjerking scene in *Forrest Gump*. Next, New York designer John Bartlett featured wildly colored Hush Puppies in his spring runway shows. "You can be good," says Bloom, "but it helps to be lucky."

The change of fortune has left Bloom feeling lucky right down to his size-13 narrow. Bloom and his marketing executives quickly canceled a series of prosaic Hush Puppies ads that were set for the fall. Instead, their advertising agency created hipper ads in a Fourth of July-weekend frenzy. The new ads showcase the colorized Duke—now renamed the "Wayne"—and the Earl on the feet of Gen X models who seem to have wandered in from Calvin Klein ads.

Some of the ads will appear in unusual places for Hush Puppies, such as *Sassy*, a teen-age-girls' magazine, and *Out*, a gay magazine. But they're really aimed at department store apparel buyers: Now that the Wayne has its suede toe in the door, Bloom wants the rest of his Hush Puppies shoes—which range from children's sandals to women's moccasins—to follow. Bloom notes that the Classics line, which includes the newly gaudy versions of the old clunkers, accounts for only about 20% of Hush Puppies sales. "The secret is to take this wonderful opportunity to command real estate we've just never been able to get," Bloom says.

**BIGGER TREND.** Of course, holding that ground won't be easy. The hot shoe this year, Hush Puppies risks being next year's fashion victim. "The world can very easily get bored with them again," warns stock analyst Sheldon Grodsky of Grodsky Associates Inc. Still, the Classics line's success is already spreading: At the Las Vegas shoe show in August, for example, Nordstrom bought Hush Puppies' new sport collection featuring techno-colored suede sneakers.

And even when day-glo Hush Puppies grow cold, Bloom is counting on the bigger trend to casual attire in the workplace to fuel more long-term sales. He has spent years restructuring Wolverine to take better advantage of that trend. When he landed the top job in



**BLOOM:** "You can be good, but it helps to be lucky"

1992—he had been COO since 1987—Bloom knew something about reviving desperately unhip fashions. As CEO of Jaymar-Ruby Inc. in the early 1980s, he's credited with putting some snap back into Sansabelt slacks for men. So Bloom quickly began refashioning the shoemaker, which had stumbled through the 1980s as Nike and Reebok sneakers became the leisure footwear of choice. "Dullness permeated the company and they just missed the entire 1980s," says Grodsky.

Bloom focused on three core lines: Hush Puppies, which account for 45% of Wolverine's sales; Wolverine work boots, which bring another 40%; and its Tru-Stitch slippers unit. "We were bleeding to death," he recalls. "I told the board we should get rid of everything that is

not comfort, work, or slippers."

Bloom's first move was to drop Brooks athletic shoes, which had been losing \$5.4 million a year. Next, he shed other unprofitable operations. Hush Puppies retail shoe outlets have gone from 176 to 60 since 1990, for example. He also slashed costs by condensing the company's 25 divisions to four. Annual revenues per employee increased by 24% in two years, to \$730,000 by 1994.

Bloom also knew Hush Puppies needed help on the fashion front, so he convinced a hot women's shoe designer—Maggie Mercado of F.H. Macy & Co. in New York—to move to bucolic Rockford. Bloom also hired fashion consultant Jeffrey Miller, former men's fashion editor at *The New York Times* and *British GQ*. Mercado's fresh style began catching the eye of influential Nordstrom buyers in 1991, while Miller's connections helped put puppies on the feet of New York's fashion elite in 1994.

The moves paid off handsomely. From less than \$5 million in 1990, Wolverine's earnings swelled to \$10 million last year. So when John Bartlett came to town in late 1994, Hush Puppies executives were ready to embrace the fashion industry that had once scorned them. The trendy designer convinced them to dye their dog to match his fall 1995 men's clothing line. The crew in Rockford liked the look so much, they launched a whole line of Hush Puppies in decorator colors. "They're hot with the fashion customer now," says Bartlett. "But they've got a huge country to cover."

That's where Hush Puppies first-class appearance in fashionable department stores comes in. Analysts expect earnings gains as Middle America begins finding Hush Puppies at the likes of Dayton Hudson Corp. To keep momentum up, Hush Puppies is also launching a line of casual suede work shoes next fall. "We have not seen the full benefit of the fashion hype," says analyst Aaron Ruth of Montgomery Securities.

The hype is still in full stride at L.A.'s Pleasure Swell. Fitzpatrick is signing lime-green corduroy trousers and "biker wallets," chain optional, topped with the shoes he sells. "Hush Puppies are going to be the flavor for at least the next year and a half," he says. Apparently, every dog does have his day.

By Keith Naughton in Rockford, Ill.

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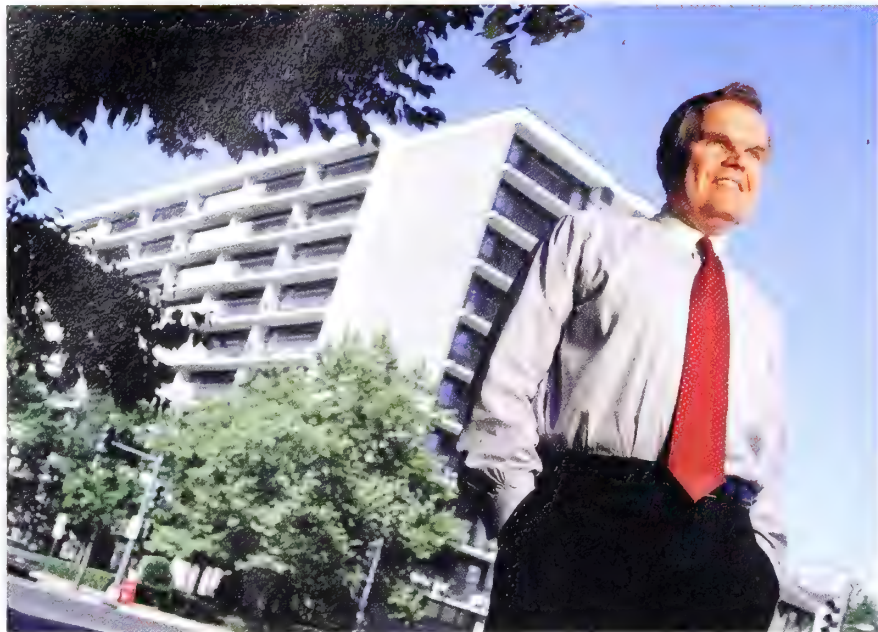


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## HOUSING

# UNCLE SAM MAY RAISE THE RENT

Subsidized housing could succumb to cost-cutting fever

**F**or 20 years, North Avenue Tower in Council Bluffs, Iowa, has been a beacon of success in the often-maligned market for subsidized housing. The apartment complex for the elderly has staff on call 24 hours a day in case of emergencies, and tenants at the six-story building are like family: Everyone hangs a doily outside their door each evening; if it isn't removed in the morning, residents check in to see if their neighbor has fallen ill.

Unfortunately, such a cozy lifestyle comes at a hefty cost—to taxpayers. More than half of the average \$505 monthly rent for the building's 100 residents comes from the U.S. Housing & Urban Development Dept. But that system could be scuttled next June when the complex's 20-year subsidy contract with HUD expires. Thanks to Congress' deficit-reduction drive, such costly agreements face the guillotine. But North Avenue Tower manager Randy Lenhoff worries that lower subsidies will put his facility out of reach for many elderly. "There will be even less choice for

low-income people in the future," he frets. "And buildings like this just won't have the same sense of community."

The repercussions of such changes will be felt far beyond Council Bluffs. Beginning next year, a wave of subsidized housing contracts under HUD's so-called Section 8 program begin to expire. But simply slashing subsidies paid on these properties could become

**DOUBLE EDGE:** CEO Heller says big subsidized-housing managers like NHP will gain an "enormous competitive advantage"

a fiscal nightmare. That's because 900 subsidized apartment buildings—value a \$28 billion—are backed by Federal Housing Administration (FHA) mortgage insurance. A drastic cut in rental assistance could trigger mortgage defaults and massive claims

on the insurance fund.

"Done badly," cautions David A. Smith, a low-income housing consultant in Boston, "this restructuring could end up costing the federal government more than it saves and doing permanent damage to residents and properties."

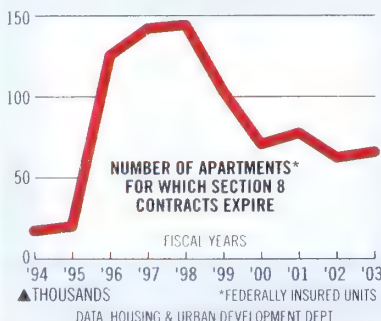
Ironically, the current dilemma stems from a hugely successful effort by the federal government to lure private capital into the affordable-housing market. Beginning in the mid-1970s, the federal government offered hefty rental subsidies to investors who rehabilitated or constructed affordable apartments for rental to tenants earning less than 80% of local median income. Many of the properties were financed by tax-shelter partnerships that relied heavily on debt. That federal-assisted housing boom yielded over 1 million privately owned apartments.

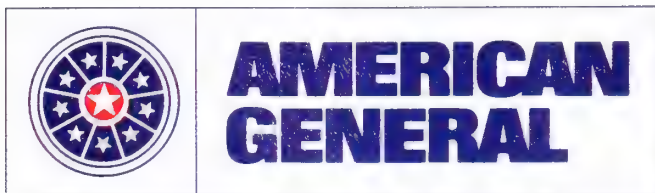
**DEFAULT DELUGE?** To investors' delight, federal aid on newly constructed buildings was hiked annually by HUD based on how local market rents were rising. But when market rents declined, HUD didn't cut the subsidies. The result: subsidized rents that in some cases are 50% above market rents. HUD officials estimate simply renewing these subsidy contracts would cost taxpayers a staggering \$222 billion over the next 25 years.

No way, say budget-slashing lawmakers. "We're in a crisis," says Representative Rick A. Lazio (R-N.Y.), who is drafting housing-reform legislation. "These subsidies will squeeze out everything else in housing." Even HUD officials agree subsidy contracts will only be renewed at market rent levels. Recapitalization Advisors Inc., which has studied the impact of such a move, figures it would send roughly 4,000 properties housing 450,000 families into default.

Fearing such turmoil, HUD is considering a proposal to form joint ventures with private investors to restructure the mortgage loans before they default. The FHA insurance fund would cap losses up to a cap based on the losses HUD would take by working out the loan itself. HUD figures its restructuring proposals would cost \$186 billion

## THE DILEMMA FACING HUD





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| Select Investors      | 16.5%  | 7.4%   | 12.3%   | 16.6%<br>(6/30/71)  | 11.7%<br>(6/30/71)               |
| Growth Investors      | 22.7%  | 11.2%  | 15.5%   | 18.5%<br>(6/30/71)  | 11.7%<br>(6/30/71)               |
| Heritage Investors    | 19.7%  | 11.4%  | -       | 16.0%<br>(11/30/87) | 15.0%<br>(11/30/87)              |
| S&P 500 Index         | 26.0%  | 12.1%  | 14.6%   | -                   | -                                |

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## Government

over 25 years, saving about \$36 billion.

The final tab will depend on how the new system is implemented, but the most uncertain is the cost to tenants. Although the aid tenants receive, potentially in the form of vouchers, will still be based on the expectation that they will pay roughly one-third of their income toward rent, some residents could end up contributing more for decent housing. And some critics worry that peeling subsidies to market rents will penalize well-run buildings in rural or inner-city areas. In such cases, rents in new apartments are very low—but often at the expense of housing quality. That could slash the demand for some better properties, causing them to deteriorate over time.

**TAX HIT.** The housing overhaul may hold an unpleasant surprise for investors. Recapitalization's Smith figure of as many as 60,000 individuals have invested in subsidized-housing partnerships. If their buildings go through a restructuring under HUD's plan, the result could be a mortgage write-down or foreclosure. In either case, the resulting write-down or forgiveness of any part of that debt to the feds could be considered a gain to investors—creating a sizable tax hit.

Low-income property owners worry that a failure to legislate a way around that tax penalty would chill the future flow of capital into affordable housing. "People who were enticed into putting their money into low-income housing may be left holding the bag," contends John E. Autry, whose firm owns and manages subsidized apartments in the Southwest.

Of course, this market turmoil may be a double-edged sword for some players. J. Roderick Heller, CEO of NHP, a big Washington-based affordable-housing manager, says his company would have "an enormous competitive advantage" and would likely gain market share as smaller, financially troubled players were forced out. But even NHP would feel the pinch: About 19% of its management portfolio is in buildings that could see declining rents, or possibly mortgage defaults, under the new regime.

Regardless of the fallout, policymakers vow to act before losses start mounting. Already, HUD Assistant Secretary of Housing Nicolas P. Retsinas says some owners are having trouble refinancing because of the uncertainty. Others are putting off necessary maintenance investments. "This is one case where inertia cannot prevail," he argues. For investors, property managers, and residents, the only certainty now is that their insulated and comfortable world is about to change—big time.

By Amy Barrett in Washington

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## COMMENTARY

By Geoff Lewis

# THE NEWTNIKS HAVE SEEN THE FUTURE. OR SO THEY THINK

**T**he name of the conference was Cyberspace and the American Dream, and the setting was ideal. Aspen, Colo., long the winter headquarters for Hollywood glitterati, is an increasingly popular haven for digerati, too. Here amid the Rockies, a growing cadre of high-end knowledge workers lives full-time—zipping manuscripts, contracts, and business plans across the Internet from million-dollar chalets.

Maybe it was inevitable that from this vantage point the 24-member panel corralled by the Newt Gingrich-affiliated Progress & Freedom Foundation would veer off the track. Or perhaps it was the composition of the group: a few computer-industry executives, some techno-pundits, several outspoken right-wing think-tankers, and one lonely government official. Whatever the reason, the view of America in the 21st century put forth by these (mainly) Friends of Newt had about as much to do with the American Dream of most ordinary citizens as Aspen has to do with Peoria.

**SECOND WAVE.** The most frequently invoked vision of the future was a society composed of yeoman information workers, trading skills and intellectual property across the Net, forming electronic communities, educating their kids online, and presumably getting as far as possible from the sights and smells of the decaying industrial world—what Newt and other fans of futurist Alvin Toffler call the “second-wave” society.

This simplistic view of cybersociety wouldn't matter much if not for the Gingrich connection. Although the Speaker wasn't there, he was the unseen star of the show. Gingrich helped host the PFF's first Cyberspace and the American Dream conference in Atlanta in August, 1994. And working with a smaller group of cyberthinkers, he helped draw up *A Magna Carta for the Knowledge Age*. This libertarian manifesto for postindustrial America was published with great fanfare as Gingrich took over the Speaker's office—and the cyber-agenda. Given half a chance, these are the folks who might wind up writing a Constitution for the Knowledge Age.

Before they do, the rest of America—business in particular—should wake up

and speak up. There was a central fallacy running through the two days of discussion: that the Information Revolution and the political revolution Gingrich leads in Washington are indistinguishable and inevitable. Just as the mainframe seems anachronistic in an era when networks of amazingly powerful desktop computers dominate, so, too, all sorts of large, centralized organizations—up to and including the federal government—are doomed to extinction. Or so the theory goes.

The father of this line of thinking is Toffler, an Aspen panelist and an influential Friend of Newt for 20 years. In the 1970s he put forth the notion of “demassification,” which basically pre-

dicted that second-wave, Industrial Age institutions that mirrored centralized control structures of a century factory would collapse. Third Wave—then heralded as the Information Age.

**CONSPIRACY THEORISTS.** The computer revolution and the growth of the Internet have made Toffler look more prescient than he has in years. And his many pupils at Aspen were quick to draw fresh corollaries. Panelist John Barlow, vice-chairman of the Electronic Frontier Foundation, a cyber-interest group, extrapolated the federal government (“a second-wave institution”) must die off as the second-wave industrial society does. Stranger to conspiracy theories, Barlow went on to predict that, facing its imminent demise, the federal bureaucracy (in collaboration with second-wave institutions such as mass media) would try to suppress the cyberspace revolution. The thing that drew a bigger response from the libertarian-leaning audience were repeated attacks on the National Education Assn. (a corrupt second-wave monopoly that has singlehandedly ruined America's education system) and calls to abolish the Federal Communications Commission.

Whether Toffler's basic premise is right is open to debate, but clearly wrong is the assertion that the decentralization of power by ruling high technology should be the guiding principle for the human endeavor. Thankful for the only Nobel laureate in the bunch, periodically yanked together, gathering back to earth. Corroborating one audience member's assertion that “we have overthrown the economic value of matter,” Penzias reminded everyone that the cyber realm is and will remain a subset of the physical world. “Let's understand there's a real world out there,” said Penzias. “I know we don't like to talk about it. But the industrial revolution will last as long as people get hungry when they come back from

## Political revolution and the Information Revolution are not one and the same





and look for something to eat." As more, there's a very real risk policies for cyberspace are made narrow, doctrinaire perspective, and society in general may lose opportunity. If vast swaths of place find the Net remains as behind reach as a trip to Aspen, the could make the Luddites look envious. And if government does a substantial role to ensure the cyberspace and mediate among competing interests (balancing the dissemination of information freely, intellectual-property rights, for example) when the new frontier will be wilderness. John Gage, Director of Science Office at Sun Microsystems and an Aspen panelist, pointed to government—and a powerful government at that—will still be only a federal government protect national security in the Information Age. In the Information Age, an assault on the Internet could cause economic havoc, the same will be. "When the devastating attack comes, when we'll want every resource government brought to bear," Gage.

**THE CORNER.** The profound impact of the technology that cybercelebrate is not in question. Nor much doubt that the absence of any interference has left hackers entrepreneurs free to experiment—order converting the Internet to an E-mail system for academics, a stew of news, electronic commerce, cyberzines, and Web sites. Next phase, however, will involve using the Net from a voluntary economy into a true commercial one where millions of ordinary Americans head for entertainment and leisure—and where businesses may find a productivity explosion by friction-free electronic markets. Nations are eager to make the Internet many will hesitate until they are sure that their assets will be safe. There's a cop on the corner to catch an electronic counterfeiters, scam artists and thieves. And if it turns out the market isn't delivering the benefits of the Net to all its citizens, people may want the government to step in to help. In short, to succeed in the cyber era, the U.S. needs to craft wise public policy—vigorous public dialogue among government, and citizens.

Editor Lewis oversees BUSINESS information-technology coverage.

## AND NOW, FOR CREATIVE'S NEXT TRICK...

After Sound Blaster, will lightning strike twice?

In the West, Sim Wong Hoo's name may not be up there in the pantheon of high-tech luminaries. But in his native Singapore, the chief executive of Creative Technology Ltd. is a celebrity. Sim has starred in a "do you know me" American Express Co. ad, became the basis of a soap opera character, and is lauded as a role model by the government. No wonder: In 14 years, Sim has turned a \$6,000 investment into a \$1.2 billion powerhouse, mainly with Sound Blaster, an add-in card featured in 70% of all multimedia PCs used in the U.S.

But the latest chapter in the Creative story is less triumphant. Sales of Sound Blaster are still growing, but margins are shrinking. Forays into new areas have proved disappointing: Sim has written off millions on stakes in voice-processing, modem, and CD-ROM companies. Co-founder Ng Kai Wa, Sim's friend since second grade, recently quit. In the quarter ended Aug. 4, the company reported a \$24 million loss as a result of write-offs on inventory and bad investments. Creative's stock has dropped more than 40% since last September, to \$10.50. "The sound-card business is slipping away," says John T. Rossi of Robertson Stephens & Co. "They need to find their next big story."

Sim says he has it: On Aug. 16, Creative unveiled the 3D Blaster, an add-in board that uses a special processor to give PCs near-TV-quality graphics. The kits, priced at around \$300, include six games to show off the technology. Sim says he'll sell 1 million units the first year: "It feels like Sound Blaster all over again."

**OPEN FIELD.** Repeating that success will not be easy. When he launched his sound cards in the late 1980s, Sim set the standard for PC audio. But with 3-D graphics, the standards are being set by Microsoft Corp.'s Windows 95. That opens the field to just about anybody. Already, creators of games are writing for PC cards being developed by such rivals as San Jose (Calif.)-based Diamond Multimedia, for example. "Everyone and

his brother will be getting into this business in the coming months," says Jay M. Wilbur, chief executive of id Software Inc., developer of the megahit Doom.

Keeping ahead of the rapidly evolving chip technology is also getting harder. Competitors are partnering with such hot Silicon Valley chipmakers as 3Dfx Interactive Inc. and Nvidia Corp. With Nvidia's chip, Diamond plans to market a single card with 3-D graphics, sound, and video this fall. Creative says it will



**SIM AIMS TO SELL A MILLION NEW 3D BLASTER BOARDS**

have an all-in-one board ready next year; for now, users of 3D Blaster will also need Sound Blasters.

What the company has in spades is market momentum: 12 million Sound Blaster customers and 30,000 retail outlets. "They've got a lock on the shelf space," says analyst Rossi, who expects the stock to rebound to \$12 by yearend.

What it lacks is fat profits. Creative still sells some 1 million Sound Blasters a month, but many are simply chips sold directly to PC makers. Sim is bracing for slower growth by revamping product development and trimming costs. "We need to work through these difficult times and build on the next generation of technology," says Sim. "What's important is to survive." How 3D Blaster fares in the market could determine whether that happens.

By Peter Burrows in San Francisco, with Helen Chang in Singapore



## SOFTWARE

# HOW DEEP IS PLATINUM'S SHINE?

Integrating the software highflier's acquisitions won't be easy

**F**lip doesn't begin to describe Platinum Technology Inc. Chief Executive Andrew J. "Flip" Filipowski, an entrepreneur whose holdings also include a recording studio, a film-production company, and 200 Boston Market restaurants. During one interview at the software company's Oakbrook Terrace (Ill.) headquarters, where he arrives clad in shorts and a loud T-shirt, Filipowski threatens to fire employees who doubt the company's strategy, jokingly propositions Executive Vice-President Paul L. Humenansky, and dismisses a question about Platinum's ability to integrate 17 recent acquisitions as "stupid."

No question, audacity has served Filipowski well so far. By snapping up a bunch of small companies in his market—software that helps corporations wring better performance out of mainframes and other computers—the 44-year-old entrepreneur is on his way to tripling revenues, to \$300 million. Wall Street, which has been mainly enthusiastic about Platinum since its 1991 initial public offering, has bid up the company's shares from the teens a year ago to around 25.

But buying companies and running them are two different things. Platinum's payroll has doubled, to 1,200, and Filipowski's team is scrambling to make its operations work as a single unit. A newly hired sales force must learn to sell unfamiliar products. More than 50 programs must be made to look and act as if they were developed by one company. And Filipowski suddenly finds himself in the big leagues, selling against such giants as IBM and Computer Associates International Inc.

**SMOOTH SEGUE.** True to form, Filipowski shrugs off the challenges and offers one of his own: to surpass \$2.5 billion Computer Associates "by the end of the decade." That's a bold boast, to say the least. Three years ago, Platinum was a niche company whose programs made it easier to use IBM's DB2 mainframe database program. But the outlook for mainframe sales began to darken in 1993, and Filipowski decid-



**JUST CALL ME "FLIP":**

*Audacity has served CEO Filipowski well*

ed to move on to other markets.

Software for so-called client-server networks was the obvious choice. In early 1991, he began a buying spree, snatching up companies whose products manage these networks of desktop clients and the server computers that feed them data and software. Filipowski acknowledges that the spree, which cost \$300 million in cash and stock, mirrors the strategy Computer Associates used in becoming the leading independent supplier of mainframe programs.

If Filipowski aims big, he certainly picks the right targets. The market for programs to manage client-server nets is growing at a 25% annual clip and could top \$10 billion in five years, says Gartner Group. Companies want soft-

ware to manage, troubleshoot, and untangle of diverse computer systems software. Answer Systems, acquired for \$38 million, handed the company a client-server "help desk" system that automates tech support. And Platinum's \$33 million purchase of Locus Computing gives it expertise in the intricacies of the Unix operating system.

Filipowski's biggest bet is the \$100 million deal for Trinzic Corp., which closed on Aug. 24. Trinzic is a top p-

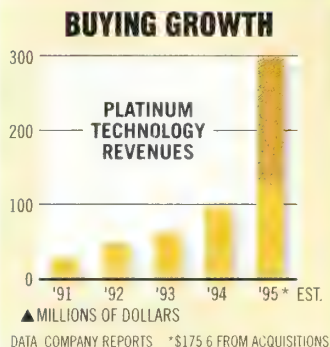
er in the fast-growing market for data warehousing—a technology for collecting information from multiple databases and cross-indexing it. By correlating data from the marketing department's server with data from engineering, for example, companies can gain valuable new insights into their businesses.

**MELDING POT.** Getting a handle on the market Platinum isn't as easy. Despite a \$1.3 million loss in the second quarter—because of a \$1 million charge for acquisition costs—analysts at Furman Selz, Robertson Stephens & Co. rate Platinum a buy. But Filipowski sees technology and marketing hurdles. A former time programmer at Motorola Inc., he now supervises the making of dozens of different programs working intimately together. "That's not an easy task," says Max P. Vason Jr., CEO of rival Software Inc.

In marketing, Platinum is no longer simply trying to persuade

midlevel managers to buy software worth \$100,000 to help run their mainframes. Now, the company must persuade technology and finance chiefs to spend \$500,000 on software that will help them organize entire computer systems. Platinum's current customers are watching this with concern. "It's a big risk, obviously," says one. The question is whether the audacity that got Platinum where it is can take it where it's going.

*By Kevin Keegan  
in Oakbrook Terrace,*





## The 1995 Business Week Conference

# The Virtual Office: Impact and Implementation



**n P. Hald** (left), chairman and founder of the IT product and service organization MicroAge, with **Raymond Adcock** (right), president Americas and marketing, Business Unit, tal Equipment poration.

**The virtual office** — a technology-enabled workplace. No walls. No boundaries. Work anytime, anyplace, linked to the people and information you need, wherever they are. Why? Because business needs it and people want it. But virtual reality is just wishful thinking unless its impact and implementation are understood. Recently more than 200 top executives and information technology (IT) specialists gathered at The 1995 Business Week Conference on the Virtual Office in New York City to talk about how to create the virtual office in their companies — and

what to expect when they do.

"It's surprising to discover how fast this phenomenon is actually taking place," says Dr. Richard Nolan, professor of business administration, Harvard Business School. "More people have virtual offices than you think."

The reasons are clear. Information — in locating customers, communicating with the sales force, creating innovative products and services — has become the most valuable corporate resource. Technology — paging, e-mail, voice mail and

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## The 1995 BusinessWeek Conference on the Virtual Office

messaging, and groupware and collaborative software — delivers it cheaply, instantly, and globally. Companies are taking out costs. Customers are better served. Employees feel empowered. And profits? "It's too early to be ultimately conclusive," says Nolan, "but it is generally positive in real cost savings, longer customer retention, and building market share."

It's changing business. Like a cyberspace Trojan horse, the virtual office is conquering the functional hierarchy from within. By enabling an intimate, immediate connection with customers, the organization can sense their needs and respond as never before. As a result, corporate structure and strategy have shifted fundamentally. "The virtual office and virtual work," says Nolan, "are transforming the old make-and-sell functional hierarchies into something entirely different, sense-and-respond IT-enabled networks."

Digital Equipment Corporation Vice-President Americas Sales and Marketing, PC Business Unit, Raymond Weadock says the virtual office began with distributed computing 35 years ago, which first gave people access to the information they needed to do their jobs. "In the virtual

### MICROAGE INFOSYSTEMS SERVICES: CUTTING THE COST AND COMPLEXITY OF CONNECTIVITY

Connectivity, efficiency, and productivity are hailed as hallmarks of virtuality. But they come at a cost—five times the initial computer purchase costs over a five-year lifetime, to be exact. And, though the cost of computer power has dropped dramatically, the costs of actually deploying technology for productivity gains more than offset the reductions.

That prompted Alan P. Hald, vice-chairman and co-founder of the IT service organization MicroAge, Inc., to alter the company's strategy. "We will remain a highly efficient multi-vendor product provider and integrator, but our focus is on growing our capacity to offer services that enhance the process improvement efforts of our clients. And since product is only 15% of the total cost of computing, we better serve our customers by spending more time on reducing the other 85% of their costs—enhancing process improvements."

Still, strategic or tactically critical activities are the corporate jewels managers are loathe to outsource. So MicroAge Infosystems Services, MicroAge's corporate account business unit, developed an alternative to the "service bundling" all-or-nothing approach to IT outsourcing—selective outsourcing. "With selective outsourcing, companies can focus on core competencies and reduce complexity, shortening cycle times, improving quality, and lowering costs," says Hald. The strategy breaks down outsourcing services into planning, implementation, and support, so companies can retain strategic or tactically critical activities and outsource non-core functions.

"I recommend that clients place IT implementation activities in a box, outsource them, manage the input, and measure the output. They'll see a big difference in their business."



A window from Apple's sales-force automation solution for Whirlpool Corporation

office," says Weadock, "the corporate structure no longer walls and space; it is the network, and shared information is the resource. It is the critical step in adapting technology to enhance corporate performance, improve efficiency, raise productivity, and lower costs."

And that's just the beginning. In companies that have implemented the virtual office, virtuality is credited with accelerating a broader rethinking of traditional business functions. Companies like GE, Ford, and Boeing have successfully applied virtual techniques in design, engineering, and manufacturing. But the most striking and widespread examples are in sales.

### Sales in Cyberspace

When mega-appliance maker Whirlpool Corporation shifted its corporate strategy to eliminate distributors and cultivate relationships with trade partners, success hinged on the sales force. But with no technological links to the central office and a lack of coordination of resources and sales support, Whirlpool recognized that to make the strategy work, big changes were needed in the field. "We needed to empower the sales force with information and presentation tools to integrate them with corporate strategy," says Ervin Barnes, Jr., Whirlpool director, IT logistics North America. Apple Computer provided the answer with a sales force automation system.

"In general sales reps need hyper ease-of-use. They're working wacky hours in all kinds of locations," says Greg Storey, account executive Apple Computer, Inc. "If the system doesn't provide immediate results, salespeople will use laptops as doorstops."

The digital sales communication solution Apple adapted for Whirlpool was designed not only to drive efficiency, but effectiveness. The Apple system equips laptops with video and

multimedia capabilities so sales reps can demonstrate commercials and print ads, tap into an online log for product dimensions and availability, work out promotional offers and discounts, and make tailored staff-training presentations at various locations.

"Our sales force cheered," attests Barnes. "Now we're introducing the system to Latin America and Europe, developing multimedia initiatives, using the system for process re-engineering." The story is similar at Hewlett-Packard. "Our people were spending too much time developing information sources and not enough time understanding the customers' needs and selling HP products," says Robert Langerman, worldwide market development manager, Mobile Computing Division, Hewlett-Packard.

But HP wanted to design and implement its sales-automation solution in tandem with business process re-engineering. For the system, it relied on its own newly created laptop division. For help with the re-engineering, it turned to KPMG and Marwick LLP, for its worldwide presence and knowledge of HP systems. Together, they set up a sales rep focus group, which set specifications for the system's development and created and tested a system prototype, Sales Information Management System (SIMS). Nine months later, the automation system was rolled out, and after a period of success in the field, SIMS is being implemented internationally.

### The Hardest Sale of All

Despite successes in corporations as prominent as HP and Whirlpool, the virtual office can be a tough sell internally. Take British Airways. There, the internal sale unfolded against the backdrop of a major sales reorganization and cost-cutting initiative. A new vice-president for sales was named, support functions were centralized, and some sales offices were closed. The reorganization put pressure on the sales force to spend more face time with the customer and strike big corporate deals in short lead times. But the existing IS infrastructure wasn't up to it. So Henry Hoffman, Jr., who at the time was senior vice-president, information management, decided to try something new — sales force automation system.

The growing sense of urgency made the sales force easy allies; selling the concept to management was the hard part. For that Hoffman developed a mini-system that would dramatize cost-and-time-saving efficiencies. To dramatize ease-of-use, he enlisted the sales VP himself, a notorious technophobe, to demo the system to senior management in London. It worked. Within five months, the pilot was generating the anecdotal and statistical evidence to suggest payback within two years. Worldwide implementation is ongoing.

"The keys to the internal sale were the buy-in of the sales department. We involved them heavily in the system's development because if it wasn't easy to use or it didn't meet their needs, they weren't going to use it."

### So What's a Manager For?

Meanwhile, the shift from workplaces to workspaces calls the very concept of "the organization" into question. Robert Johansen, director, emerging technologies program, Institute for the Future, likens the post-re-engineered organization to a fishnet: edge-oriented and amorphous, flexible, fast, and vast.

Managers, left at the center, are slow to embrace the virtual organization and reticent to yield control to the edges. Beyond yielding control, Johansen says the real virtual management challenges are maintaining continuity, building cooperation, and safeguarding organizational memory — in essence building a "telecommunity."

Adelaide Horton, managing director, Chiat/Day, who marshaled that advertising agency's cyber-shift, says virtuality requires a wholesale reorientation of management. "Management tends to hang on to supervision. It's a difficult leap of faith to move from management as supervision to management as access." Horton says the impact on human and group dynamics is significant. "People still need to be together. So in the virtual office, the underlying motivation behind management, whatever its structure, should be to champion that, and, in so doing, enhance a community of knowledge."

But that's the best scenario. Arlene Johnson, vice-president, Families and Work Institute, cautions that culture changes could lead to weaker interpersonal relationships, more formality, and "forced flexibility."

"How the 'flexplace' affects corporate culture depends to a great extent on whether human factors are a conscious part of planning for a virtual office environment," says Johnson.

"People are the killer application," Jerry

## The 1995 BusinessWeek Conference on the Virtual Office



**John M. Paul**, senior vice-president, product and business development, Banyan Systems Incorporated



**Robert Langerman**, worldwide market development manager, Mobile Computing Division, Hewlett-Packard

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**The 1995  
BusinessWeek  
Conference  
on the  
Virtual Office**



**Richard Lush**, director of network marketing, Digital Equipment Corporation

Michalski, managing editor, *Release 1.0*, reminds executives. "Technology is only valuable if it enables people to communicate and perform better."

So Johansen stresses the importance of setting serious human resources policies to regulate overwork. "While the promise of the virtual

organization is work happening anytime, anywhere, the danger is that it will happen every time, everywhere." Making it clear that, in its implementation, virtuality is a human drama still unfolding.

By Martin Keohan in New York.

## IT'S REMOTELY POSSIBLE

Virtuality is spreading us wire thin. And until now, remote users have been shortchanged. Whether away from their desks or out of the country, they were out of the loop. Not anymore.

"The critical component supporting virtual offices is the network," says Richard Lush, vice-president Digital Equipment Corporation. "Now, responding to a growing need in business for cross-departmental teams, technology is enabling *virtual networks*." Since virtual teams are usually temporary and geographically dispersed, wiring them is expensive and ineffective. But technological innovations like Digital's RoamAbout Access Point enable wireless connectivity for roaming workers who need constant access to the network—from anywhere within 800 feet.

For the even more remote, NetRider, another Digital innovation, offers remote users a complete (hardware and software) access solution. Using dial-up technology, users enjoy full access to file servers, databases, printers, e-mail, and other network resources. NetRider also provides unprecedented ability to either drag a file remotely from the network or to tap into the network capabilities directly. "This kind of total access allows remote users to be full members of a virtual team," says Lush.

And just as networks evolve to meet the demands of the remote user, the notebook itself is evolving, adding speed and flexibility to the road warrior's arsenal. Innovations like NEC's Versa 4000 Series combine the power of the Pentium processor with the flexibility of modularity to catapult the laptop into a new era of functionality. "What we're offering remote users is true flexibility—high-end

power to handle demanding jobs, plus modular design so end-users can upgrade, reconfigure, and expand the notebook to fit their daily agenda," says Bob Levin, director of product marketing for NEC's Portable Systems Group.

Of course, keeping track of all these innovations means managing multivendor, multiprotocol enterprise networks—a daunting task. But it doesn't have to be. To find, share, and manage information, John M. Paul, senior vice-president, product and business development, Banyan Systems Incorporated, outlines Banyan's threefold REDWOOD strategy: "Enable users to find, access, and share the information they need, wherever it is in the extended network; use electronic mail and the Internet to extend the reach of corporate database applications to remote users, partners, and consumers; and automate routine, labor-intensive administrative tasks so you can be more proactive in network and systems management."



NEC displays its Versa Series

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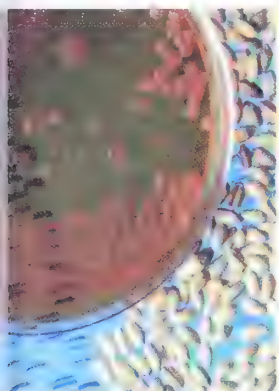
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## S WHEAT NGUS MET MATCH?

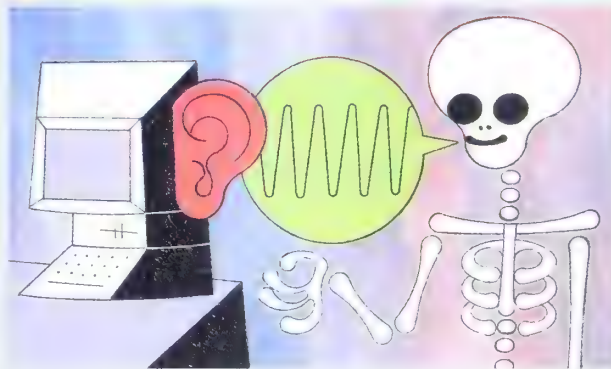
EAT FARMERS MAY SOON use biotechnology to take on "take-all," a fungus that attacks the roots of wheat plants, turning them black as it attacks them alive. Take-all reduces wheat yields by an average of 15% in the Northwest U.S., where moist soil conditions favor fungal growth.

The biotech battle against take-all began in 1988, when the Agriculture Dept. researchers identified a natural antibiotic produced by soil-dwelling *Pseudomonas fluorescens* bacteria. The researchers isolated the genetic coding for the



antibiotic in 1992. Since then, researchers have placed the genes from other strains of *Pseudomonas* that are better suited for agricultural wheat-growing conditions. They have also learned to mass-produce the bacteria and coat them onto wheat seeds in batches as large as 1,000 pounds. "It is coming together," says James Cook, research leader for the USDA's Root Disease & Biological Control Research Unit in Pullman, Wash.

The USDA is about to settle on choosing a commercial partner to aid in its quest for a needed Environmental Protection Agency approval. Cook expects commercialization of the process within a few years.



## A BETTER WAY TO SPOT BRITTLE BONES

ANDREW D. DIMAROGONAS FIRST USED VIBRATION ANALYSIS in the 1960s while at General Electric Co. to detect flaws in turbines and rotors. Now, he is using it as an easy and cheap way of diagnosing osteoporosis.

The brittle-bone disease that affects more than 20 million Americans, mainly middle-aged and older women, has until now been checked primarily with X-rays. Dimarogonas uses ordinary sound waves in the audible range that rise in pitch. If the signal that bounces off the bone is damped, or softened, it indicates brittle bone. Since the device is easy to handle—the final version is expected to be the size of a fountain pen hooked up to a notebook computer—"we can measure almost every bone in the body," says Dimarogonas, who is now a mechanical-design professor at Washington University in St. Louis.

The patented technology has been licensed to Eko Medics Inc. of St. Louis, which is owned by a partnership between Washington University and venture-capital firm Alafi Capital Co., based in Berkeley, Calif. Clinical trials aiming at Food & Drug Administration approval should start within 18 months. Dimarogonas hopes the device will hit the market in three to five years, at a price of \$10,000 to \$20,000, in contrast to \$100,000 to \$300,000 for an X-ray machine.

## RECYCLING CHLORINE: A RECYCLED IDEA

SWIMMERS PLUNGING INTO public pools often feel reassured by a whiff of chlorine. But the chemical is an environmental nightmare.

American makers of plastics, paints, and other materials consume 12 million tons of it each year. During production, as much as half of that may combine with hydrogen to form a corrosive waste, hydrogen chloride, which turns into hydrochloric acid when dissolved in water.

Soon, companies may be able to recover the chlorine from waste hydrogen chloride and reuse it, thanks to a refinement of a 130-year-old catalytic technique for cleaving chlorine and hydrogen bonds. The original approach converted only 70% of the hydrogen chloride. And the high costs of handling the hot, corrosive mix-

tures prevented commercialization. But University of Southern California researchers have broken the catalytic process into two steps that run cooler. Based on 18 months of tests with Carburos Metalicos in Barcelona, USC chemical engineer Ronald G. Minet says they can recover chlorine for just \$80 per ton. The chemical costs as much as \$250 per ton on the open market. Chemical giant ICI and others have expressed interest.

## INTEL MAY HAVE GIVEN ITS RIVALS A BREAK

EACH NEW GENERATION OF microprocessors from Intel Corp. usually doubles the speed with which personal computers can run programs. Not this time, though. Intel's own tests show that many existing Microsoft Windows programs will operate some 16% slower on the P6—the code name for Intel's next-generation microprocessor due out this fall—than on high-end Pentiums.

The reason: Intel tuned the P6 for programs written for such advanced operating systems as Unix and Microsoft Corp.'s Windows NT, which process 32 bits of data at a time. To save valuable space on the new chip, Intel left out transistors that would have speeded up older 16-bit programs. Even with the initial version of Microsoft's Windows 95, the P6 outruns a high-end Pentium by only 25%.

That could give rivals such as Advanced Micro Devices Inc. and Cyrix Corp. a window of opportunity, since their next-generation chips are designed to speed up 16-bit code as well as 32-bit code. But by 1997, when the P6 will be in high-volume production, 32-bit programs may dominate.



## CHEMISTRY

# WEIRD FLUIDS, BIG BUSINESS

Supercriticals may be reaching critical mass

**N**utraSweet Co. puts eggs through the wringer to make Eggcellent, its new egg-yolk powder with 74% of the fat and 90% of the cholesterol removed. It dehydrates them, turning the golden spheres into a powdery glob. Then, it shoots in carbon dioxide that has been transformed under high pressure into a so-called supercritical fluid. This liquid-like gas becomes a dieter's best friend, extracting fatty triglycerides and cholesterol but leaving phospholipids—the fats that help foods stick together. Introduced late last year, Eggcellent is showing up in grocery items ranging from waffles to mayonnaise.

As NutraSweet's success shows, supercritical fluids are finally delivering on some of the high hopes of the 1980s, when supercritical decaffeination stirred excitement. These mysterious fluids—actually gases or liquids that turn into a new state of matter above a "critical" temperature and pressure—are being used or tested for such varied applications as distilling petroleum and destroying U.S. Army tear-gas stockpiles.

Why are supercritical fluids finally reaching critical mass? For starters,

tougher standards for air and water quality and food and drugs have pushed industries toward the ultraclean technology. Engineers have also learned from years of high-pressure experimentation how to coax desired properties from supercritical fluids by tweaking their temperature and pressure. Getting Eggcellent out of egg yolks "took more hours than I care to remember," says Kenn Vest, the product's marketing development director.

Scientists have known since the late 19th century that certain materials took on strange properties when sufficiently heated and squeezed. Carbon dioxide, for instance, goes supercritical at 88°F and 73 times normal atmospheric pressure. Above that point, it has the density of a liquid but behaves like a gas in the way it diffuses into cracks and crevices. It's a gentle but effective solvent. Supercritical water is something else entirely: Mix it with oxygen, and the combination oxidizes nearly anything it touches—the same as fire.

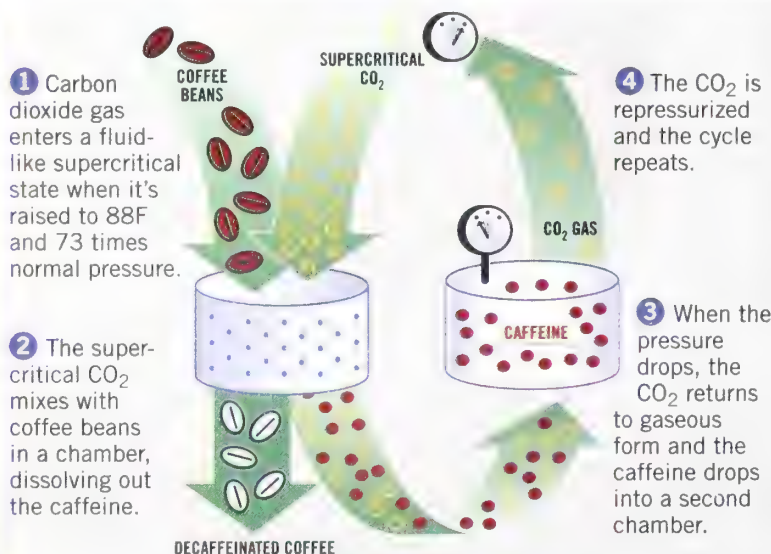
The petrochemical industry was first to exploit supercritical fluids. Beginning in the 1950s, it used a supercritical version of the hydrocarbon gas pentane to distill heavy crude oils and tar. In the late 1970s, German coffee company HAG mastered the use of supercritical carbon dioxide to decaffeinate coffee. General Foods Corp. bought HAG in 1979, and in 1988, its Maxwell House Coffee Co. unit refitted a plant in Houston for supercritical extraction (diagram). Decaffeination used to depend on methylene chloride, which is now a suspected carcinogen. The other big decaf maker simply switched to another chemical; Maxwell House says it picked supercritical extraction for Sanka and other brands because it better preserved the coffee's flavor—and adds that its customers are pleased.

**TEFLON AND SPRAYS.** The 1990 amendments to the Clean Air Act are giving supercritical fluids a boost by requiring the phaseout of chlorofluorocarbons. Supercritical carbon dioxide could substitute for CFCs in the making of fluoropolymer plastics such as DuPont's Teflon. In production of emulsion polymers such as polyvinyl chloride, the building blocks called monomers don't always mix well in supercritical fluids. Joseph M. DeSimone, a University of North Carolina chemist, is leading research on a kind of chemical "soap" to improve the mixing. Aside from polymer production, supercritical fluids can be used to create evenly sized, microscopic particles from substances dissolved in them. Phasex Corp., Lawrence, Mass., and Dura Pharmaceutical Inc. of San Diego are exploiting that property to create better inhalable drug sprays.

In environmental cleanup, water is the most promising of the supercritical fluids. Last year, Eco-Water Technologies of Austin, Tex., completed the world's first commercial system to treat wastes by supercritical water oxidation. Running at 1,000°F and 21 times atmospheric pressure, it treats about five gallons

## The Clean Way to Make Decaf Coffee

Coffee decaffeination used to employ harmful methylene chloride. Now, Maxwell House Coffee Co. uses a "supercritical" form of carbon dioxide, a harmless gas.





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liquid waste per minute at a laboratory and pilot plant in Austin owned by Huntsman Corp. Such harmful organic materials as benzene, hexane, and acetone are turned into carbon dioxide, water, hydrogen, nitrogen, and pure water, with small traces of carbon monoxide. Huntsman says the process costs about \$1.25 per gallon that it pays for incinerating the liquid waste. So far, the system won't work on any chlorinated or fluorinated compounds, such as carbon tetrachloride. **MULTIPURPOSE?** For the U.S. Defense and Energy departments, an environmentally friendly way to wipe out harmful wastes could be a big business. One U.S. Navy officer estimates that the Defense Dept. alone could use up to 25 supercritical-water-oxidation plants, each one handling 6,000 gallons a day. Indeed, Defense and Energy are spending \$15 million to \$20 million every year just to develop the technology.

## WHERE SUPERCRITICAL FLUIDS ARE USED

| PROCESS                                      |            |
|----------------------------------------------|------------|
| DECAFFEINATION OF COFFEE                     | LATE 1980s |
| REMOVAL OF FAT AND CHOLESTEROL FROM EGGS     | 1990s      |
| TREATMENT OF LIQUID INDUSTRIAL WASTE         | 1990s      |
| CREATION OF MICROPARTICLES FOR DRUG INHALERS | RESEARCH   |
| POLYMER PRODUCTION                           | RESEARCH   |
| DATA: BUSINESS WEEK                          |            |

They are cooperating with other companies as Foster Wheeler Development, Martin Marietta Energy Systems, and Modell Development based in Framingham, Mass.

Enthusiasm for supercritical fluids may overreach at times. For instance, Los Alamos National Laboratory and Hughes Environmental Systems may be spending \$3 million to study the use of supercritical carbon dioxide for dry cleaning as a substitute for harsh perchloroethylene. But corner dry cleaners might be better off simply picking a less-harmful chemical solvent. Phyllis Kruk, founder and President Val Krukonia, guesses that supercritical fluids aren't needed for most kinds of cleaning. For example, Charles A. Eckert, a chemical engineering professor at Georgia Institute of Technology and vice-president of the International Society for the Advancement of Supercritical Fluids, says supercritical fluids should be "a tool, not a goal." Still, in several fields, this high-pressure state of matter could take the place of pressure off the environment.

By Lars Hansen in New York

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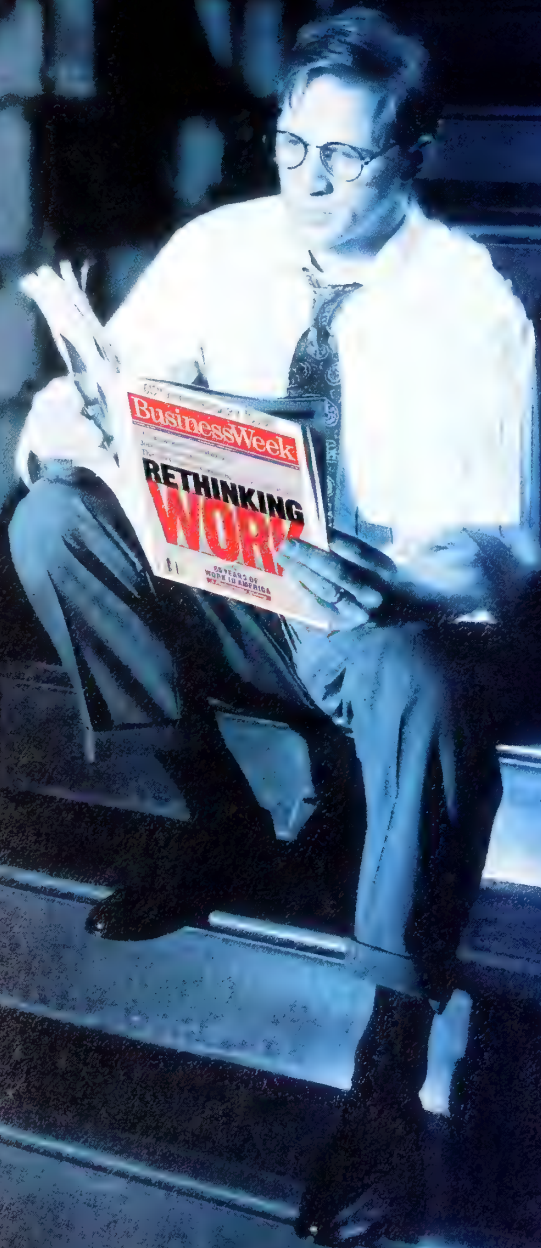
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# THE TOWN IBM L

## Around Poughkeepsie, Big Blue's fading seemed fatal. Here's why it wasn't

**I**BM was... it was great. You should have been here to see it. They could spend money, they were like the government. We'd get a multimillion-dollar job done, and before you knew it, they'd rip it out and start something new. We thought it would never end.

—Ronald J. Weiss, C.B. Strain & Son, mechanical contractors

On the morning of Mar. 30, 1993, the world's biggest computer company announced what many in New York's Hudson Valley had feared in their guts, but few had really thought possible: "2,700 Fired," the *Poughkeepsie Journal* mourned. IBM already had drained thousands of jobs from the region in the previous five years. But this was a crushing blow: For the first time in its history, Big Blue was laying people off.

"It was really devastating to everyone," recalls Yvette Wild, a line worker who lost her job that day. What had been

the valley's dominant employer ultimately would reduce the

## Special Report

payroll at three local plants by two-thirds from its 1984 peak of 31,300 jobs, abandoning a mammoth chunk of its East Fishkill factory and shuttering another in Kingston, 20 miles upriver. The reason was no mystery: IBM had lost \$16 billion over three years. Its products in many markets were uncompetitive; its rivals simply were better.

More than two years later, Poughkeepsie and the villages that dot Dutchess County's surrounding hills still suffer from the resulting dislocation. Howard Aronoff, once a senior planner for IBM's mainframe software, is retired at age 55. Although a generous severance package keeps him above water, he hasn't found the sort of work he spent a career doing—and "I refuse to pack cans in a grocery store." Doug Bradley, who used to

### HANGING IN

“Some people are paying, some aren't. Money is tight—let's face it”

— MIKE ZDRODOWSKI  
Owner, Mike's Lawn Mower, in LaGrange, N.Y.



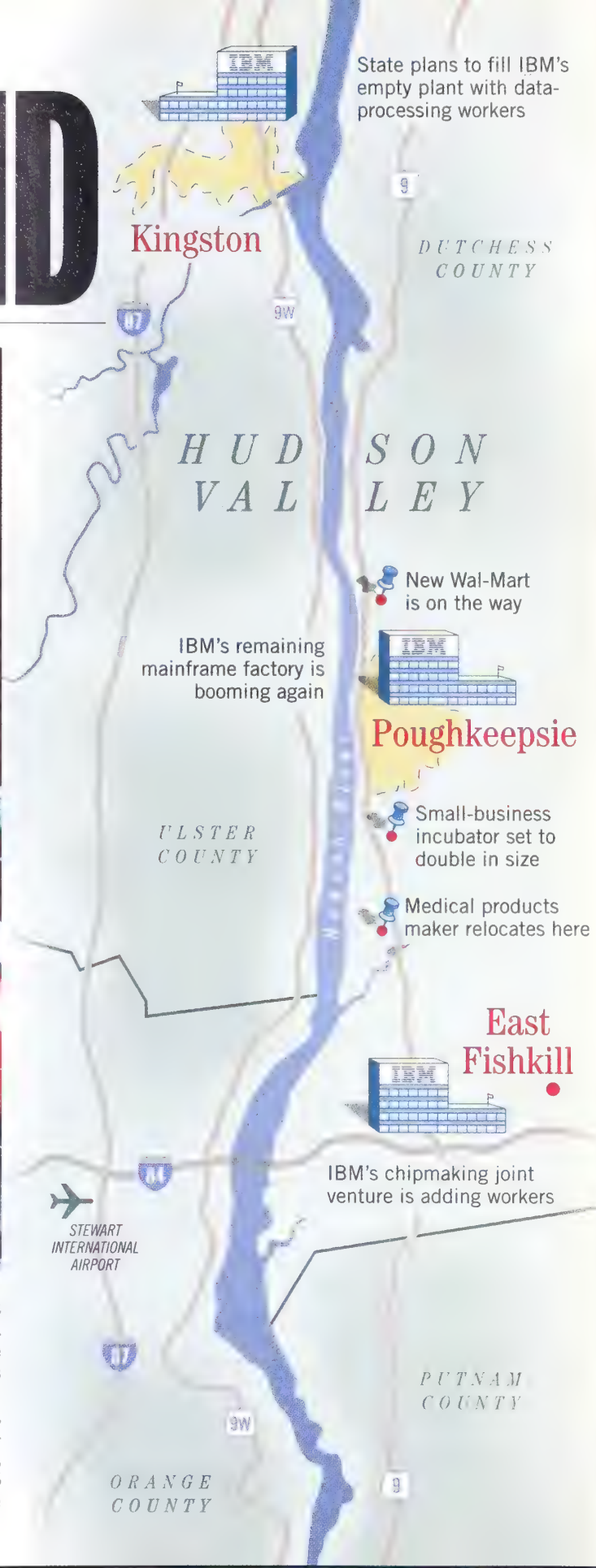
clean IBM's floors, does odd jobs and gets lunch at a kitchen. At Mike's Lawn Mower in LaGrange, N.Y., Zdrodowski's business is off 40%. "Some people are paying, some aren't," he says. "Money is tight—let's face it."

IBM's downsizing, in fact, has cut deep into this community of 75 miles north of New York City. Yet the shock also has led to something fairly remarkable: The high-tech company that once was the lifeblood of the area now lacking its company, is finding a new energy of its own. A wave of industrial migrants is filling some of the empty properties that form a necklace of "For Rent" signs around

# T BEHIND



region, won over in part by an activist government that had the luxury of thumbing its nose at development. Tech startups are retooling the clean rooms IBM once to manufacture microprocessors; mom-and-pop operations found happiness in old IBM research space. Entrepreneurship is blossoming where once, "everyone, where had the same big-company mentality," says Robert Ritter, 35, a frenetic young executive who, in a year, built a thriving small-business incubator nurturing 35 startups. Fayiz Hilal's Cetek Inc., a 22-employee machine







Folks were in denial—sure that another big computer outfit would move in soon

shop, lost more than half its revenue in 1994; now, Hilal is developing a new ceramics process technology. "Once we're set up to get sufficient production out the door, we'll be sold out," he pledges. "Sold out."

The Hudson Valley has embarked on a quest to regenerate itself—to survive and retain viability in this era of global competition. It is a struggle that resonates in cities and towns throughout the nation. Can communities save themselves from economic and social irrelevance? How do they sustain competitive advantage? "International capital can go anywhere it wants," says Harvey K. Flad, a geographer at Vassar College in Poughkeepsie. What will bring it here?

The answer, the valley is discovering, is complex. Government, certainly, must buy in: Its actions can nurture development or choke it. Regional linkages, too, are crucial. The Information Age notwithstanding, companies locate or expand in places where there are suppliers and buyers. Most important of all is human capital—an educated workforce that can keep up with unyielding market change.

**NO PRISONERS.** What's at stake, in essence, is quality of life. The global economy is acting relentlessly and decisively on American communities, forcing them to do battle with Singapore, Mexico, and one another for jobs and wealth. Yet how cities and towns respond to that challenge produces quintessentially local, human effects. Strategies for development, or lack thereof, determine whether homes will gain value; whether the playground will be maintained; whether people will plant roots or flee to a place with better prospects.

Dutchess County has begun to create a new competitive machine. The cooperative effort of business and government has yielded impressive early results, producing a substantial foundation for recovery. The region won't ever bring back the heyday of IBM. Indeed, few here want that. What most envision is something far more potent: a diversified economy yielding sustainable, high-wage employment.

The alternative is a region little more than another spot on a map, an also-ran with low-skill service jobs, a McDonald's and a Wal-Mart. An also-ran that used to have it really go-

The company town is a fundamentally flawed economic organism. We have known this for decades, with grim testament in the collapse of Rust Belt industrial centers. Think U.S. Steel and Homestead, Pa., or General Motors and Flint, Mich. (page 112). Dominant employers foster dependency in their communities, dulling the incentive to take risks. Give captive labor and suppliers, moreover, companies themselves typically lose their edge. "The model is not conducive to growth," says Edward L. Glaeser, an economist at the Hoover Institution on War, Revolution & Peace. "Diversity and competition are the linchpins to long-term profitability."

But the truth is, company towns are irresistible. Big employers create complacency, but also jobs. They build schools and pay doctors' bills. "People always say, 'Don't put your eggs in one basket,'" says Emerson L. Burger, a project manager laid off when his employer, a Poughkeepsie engineering firm, went under with IBM's cutbacks. "But when they're a major employer in the area, it's awfully hard not to."

**WAR MARRIAGE.** IBM arrived in the Hudson Valley in 1941, setting up shop to make aircraft cannons during the war and, afterward, office equipment. The place appealed as it had earlier industrial migrants: Land was cheap, labor was skilled, the mountains looked nice, and a solid transportation infrastructure linked the area to major Eastern markets. By the mid-1960s, Poughkeepsie and Kingston were at the heart of a spectacularly successful mainframe-computer business.

For four decades, IBM thrived—and the Hudson Valley

## Lessons from Dutchess County

**DIVERSITY EQUALS VITALITY** A region dominated by a single company or industry is ripe for disaster. Think of it as sound portfolio management: With a broad base of industry, one failure won't kill off the local economy.

**PEOPLE POWER** It's impossible to compete globally without a skilled workforce. Companies won't move in, and entrepreneurs will go elsewhere.

**LOCATION, LOCATION, LOCATION** Yes, everyone can do business by fax, phone, and Internet, and companies can sell to anyone, anywhere. But most still depend on a regional network of suppliers and customers to keep them going.

**TRANSPLANTS ARE OVERRATED** Luring new companies to the region is a quick way to bring in new jobs, but it's an expensive fix. Better to retain existing businesses and to nurture entrepreneurs.

**GOVERNMENT HAS A ROLE** An aggressive development strategy can trigger growth. Longer term, though, human capital, infrastructure, and market forces are more important.

**GROWTH TAKES TIME** Economic recovery doesn't happen overnight. The challenge: Keeping critical resources in place and motivation high until development efforts create broad, sustainable gains.

boomed. Kids got high-pay manufacturing work out of high school. Developers devoured dairy farms around Poughkeepsie, building offices for IBM and housing for the engineers and managers flooding in. Home prices soared, as did wages. "Benign," as the locals called the populated local zoning boards, ran charities; their money funded a vibrant retail sector. And companies that supplied IBM with parts, engineering services, food and landscaping slipped into comfortably monogamous relationships with their big benefactors.

All of which made the crash when it arrived, that much more cataclysmic. "There was disbelief," says Louis W. Quaresimo, president of Local 201 of the Plumbers & Steamfitters Union. "People thought some other computer giant was going to come in, and everything would be back to normal. It took months to realize what was happening." By then, in late 1980s, unemployment in Dutchess County had reached 10.8%, from 3% in 1990, and business failures were soaring. Some 10% of Quaresimo's members were out of work, even after accepting a 25% wage cut. The home market collapsed; the Porsche dealer shut down.



# Hope on the Hudson

DATA: MARIST COLLEGE BUREAU OF ECONOMIC RESEARCH, NEW YORK LABOR DEPT., NEW YORK TAXATION & FINANCE DEPT.



The company town didn't fold. In fact, the sense of crisis gradually ebbed, and the support groups in church basements for unemployed engineers quietly disbanded. Newcomers rushed to fill the newly cheap homes, cushioning the real estate market and retail sales. For the county, being two hours from New York City and its job engine became a fortuitous geographical blessing.

But there was a perilous downward spiral in the making. The new residents, who mainly commuted to work south of the county, did nothing to expand local employment. Instead, they kept seeping out, as successive waves of suppliers shut their doors. The risk grew that the shrinkage of the region's industrial base would perpetuate itself, placing increasing pressure on residents and remaining businesses to support strained government services. "There's a ripple effect," says

Paul J. Ganci, president of Central Hudson Gas & Electric Corp. "You risk losing everything that's a fabric of the community. That was scary."

**BIG PHONE BILL.** As IBM mapped out its restructuring early in 1993, a few local leaders began making their own plans. Ganci and T. Jefferson Cunningham, a banker, buttonholed other business executives—senior IBMers among them—for donations to revitalize the county's marketing efforts. They raised \$450,000, got the county and state to add \$500,000, and commissioned a study of the region's resources. The primary recommendation: market the dozens of empty IBM sites scattered around the county as low-cost alternatives for New York area companies.

## Special Report

With that, Kathleen Sullivan Norat went into action. Sullivan Norat, now 38, was regional director for the state's Economic Development Dept.—the area's chief marketing officer, in effect. In dozens of calls each day to prospective tenants all over the country, she pitched the valley's human resources, the network of suppliers, and the extensive communications infrastructure. She talked of a "global company town" from which companies could do business anywhere.

Her strategy: prime the pump. Bring in state and local monies to start businesses and bolster existing companies. Pursue high-wage, high-skill jobs, "because low-wage jobs are probably going to go elsewhere anyway, and they're not going to build back the economy," she says. And target smaller employers, leaving to deeper pockets the giants that demanded huge public incentives. A few successes would encourage others, setting the stage for broader recovery.

In some ways, the region was an easy

## PURSUING SKILLED WORK

“Low-wage jobs are probably going to go elsewhere anyway”

—KATHLEEN SULLIVAN NORAT  
Dutchess County development official



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sell. For starters, almost everything IBM had built and bought over 50 years was still there. The company brass took 20,000 jobs out of the valley, but they left the custom desks and bookcases behind rather than pay to move them. They left the raised floors, with miles of fiber-optic cable underneath, and the world-class clean

## Special Report

rooms, power plants, and chemical-disposal facilities.

For Richard Borstelmann, it was "like living in the Plaza after staying at the Y your whole life." His 10-person company, UCE Inc., moved to the East Fishkill plant in March from cramped quarters in Norwalk, Conn., to make custom liquid-crystal displays in IBM's clean rooms. Down the hall, Gary and Susan Jones are reveling in the IBM evaporators—\$5 million, two-story-high pieces of equipment—that they got cheap and fast. Their three-year-old FED Corp. makes advanced flat-panel displays; moving from North Carolina to the IBM space, with its elaborate trappings already in place, saved at least a year in getting their displays to customers.

**HUGE LOAN.** There's a catch, though. While it was IBM that initially attracted the new talent, taxpayers will end up helping to bankroll the resulting jobs. The East Fishkill site is one of three state economic-development zones in the county. By relocating there, FED and UCE qualify for a seven-year property-tax abatement, not to mention investment-tax credits, sales-tax refunds, and wage-tax credits. Other state and local programs tie grants and low-interest loans to concrete job-creation targets.

In all, \$60 million in state aid flowed into the Hudson Valley in 1994—more than the region had received, cumulatively, in all its history. (Sullivan Norat, say admirers, is expert at beating the bureaucratic money-bushes.) Some \$40 million of the total was lent to Micrus Corp., a new chipmaking joint venture of IBM and Cirrus Logic Inc. that promised to keep 400 jobs in East Fishkill and add 300 more over two years. An additional \$8 million went to retrain former IBM employees.

Such incentives, widely used in regional development, create an attractive hook for out-of-towners looking to site a plant. Yet the payback, in terms of incremental tax revenue or consumer spending, is difficult to pinpoint; indeed, it's not clear whether, ultimately, they create much economic value at all. "I always think those actions might affect things at the margin, but they don't create recovery or decline," says Matthew Drennan, an economist at New York University.

More to the point,

the money won't last forever. Now past its crisis, the valley likely will see a small fraction of its 1994 windfall this year. The state likely will turn down Cirrus Logic's request for \$10 million grant to enlarge Micrus, which will expand anyway.



This is entirely appropriate. "Do we need special attention now? No," says Sullivan Norat, who in January became president of Dutchess County's Economic Development Corp. (EDC). Far more important, in any case, are the resources that will remain after the tax abatements run out. Highways, Airports. And, more than anything, suppliers. Fax machines and the Internet may foster global business ties, but having a crucial vendor just across town is still what counts most. "Here, we can get custom parts machined at 2 a.m. if we need it," says FED's Gary Jones. "Anywhere else, we'd have to fly someone to San Jose."

Indeed, a big part of Sullivan Norat's successful pitch

## The Valley's New Face

### NATIVE SONS

| COMPANIES ESTABLISHED IN DUTCHESS COUNTY BEFORE IBM'S 1993 LAYOFFS | PRODUCT                         | JOBS |
|--------------------------------------------------------------------|---------------------------------|------|
| MICRUS                                                             | Chipmaking joint venture        | 700  |
| TEXACO                                                             | Research & development          | 550  |
| WELLCARE                                                           | Health-maintenance organization | 370  |
| FARGO MANUFACTURING                                                | Power line equipment            | 220  |
| CONKLIN INSTRUMENT                                                 | Telecommunications equipment    | 175  |

### MIGRANTS

| EMPLOYERS LURED TO THE AREA SINCE 1993 | PRODUCT                             | JOBS |
|----------------------------------------|-------------------------------------|------|
| LAERDAL MEDICAL                        | Medical products                    | 165  |
| H.O. PENN MACHINERY                    | Construction-machinery distribution | 75   |
| DATA COMM MGMT. SERVICES               | Telemarketing                       | 71   |
| FED CORP.                              | Flat-panel displays                 | 55   |
| COLOR COMMUNICATIONS                   | Color-sampling products             | 15   |

### AND STARTUPS

| TENANTS AT THE COUNTY'S BUSINESS DEVELOPMENT CENTER INCUBATOR | PRODUCT                        | JOBS |
|---------------------------------------------------------------|--------------------------------|------|
| SOLID STATE COOLING                                           | Thermoelectric cooling systems | 6    |
| HAM CENTRAL                                                   | Amateur radio sales            | 3    |
| GLOCAL-VANTAGE                                                | Management consulting          | 1    |
| DOVER MEDICAL COMM.                                           | Health-care education programs | 1    |
| HITPOINT AUDIO                                                | Sound for video and multimedia | 1    |

DATA: DUTCHESS COUNTY ECONOMIC DEVELOPMENT CORP.

In 1994, the reeling area received more state aid than it had in its entire history.

Laerdal Medical Corp. was her promise to create a medical-product supplier network. Stethoscopes in IBM-lab coats. The EDC worked with the Hudson Valley Technology Development Center, a state-funded nonprofit group, to identify machine shops and other vendors that could supply Laerdal parts and services. With a \$135,000 state grant, the EDC also has begun an initiative to link large companies with area suppliers that can take on outsourced operations.

The point is twofold. First, diversity feeds itself. Second, while reported talent is nice, it's at least as important—and a lot cheaper—to take care of the resources a community already has. That means creating an environment that will induce remaining employers to stay put—a concept that high-tax New York's still struggling with. The private sector is



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(“SANWA BANK. 人尽皆知, 亚州业务, 首屈一指, 历史悠长。” is Chinese for, “Of course I know Sanwa. They have been a key part of our business in Asia for years.”)



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# TRY AS THEY MIGHT, THE DEAD SELDOM RISE

It was the prototypical steel mill, a 400-acre, 3,000-employee testament to American heavy industry. But U.S. Steel Corp. shut down the Homestead Works in 1986. Repeat-

## Special Report

ed efforts since to attract new employers to Homestead, Pa., including Sony, Mercedes-Benz, and United Parcel Service, have failed. Today, half of Homestead's households earn no money. Its middle class has fled, and the struggling town of 6,000 along the Monongahela River is overrun with poverty and drug gangs.

It's an all-too-familiar picture: The American landscape is littered with hardscrabble towns that withered away when the big employer went bust, relocated, or laid off thousands of workers. Gary, Ind.; Brockton, Mass.; Darlington, S.C.—the names might as well be engraved on tombstones.

**RUSTY SKILLS.** As Homestead has found, a host of obstacles can frustrate recovery. Competition among cities to land large employers is fierce. Too often, old company towns, encumbered by high wages, unionization, and creeping urban decay—not to mention little wherewithal to offer financial inducements—can't win. Just as important, the

skills of local workers, coddled by years of job security, may be out of touch with the times. "We are sadly unprepared," says Mary Flagg, Homestead's borough manager.

Flint, Mich., for example, tried luring new business to town when local kingpin General Motors Corp. started shutting plants in the late 1980s and unemployment soared to 22%.

Its problem: a dearth of workers trained to do anything but assemble cars. The redevelopment effort stumbled, as did an attempt to diversify by opening a combined museum/theme park called Auto World. And Flint, with its crime and boarded-up shops, isn't exactly a magnet for corporations. Unemployment has dropped—to 12%—only because GM is hiring again.

Lack of infrastructure and regional linkages can kill off development efforts, too. The once-bustling timber town of Klamath Falls, Ore., has had little success bringing in new business to replace 2,500 well-paying jobs lost since 1979, when mill owners such as Weyerhaeuser Co. began closing shop. Its problem: location. Situated about 17 miles from the California border, it isn't near any big cities. It isn't near a big airport. It isn't near anything.

Those towns that do win fresh employers are

finding the new jobs don't pay what the old jobs did. Eau Claire, Wis., has struggled mightily to replace 1,500 jobs lost when Uniroyal Chemical Corp. closed its plant in 1992.

The town has attracted dozens of small startups and recently landed Hutchinson Technology Inc., a maker of computer disk-drive parts, which plans to open a 156,000-square-foot factory employing 1,400. But few of

## Company Towns Minus Companies

| TOWNS               | DEPARTING COMPANIES     |
|---------------------|-------------------------|
| LACKAWANNA, N.Y.    | Bethlehem Steel Corp.   |
| RIPLEY, OHIO        | U.S. Shoe Corp.         |
| EAU CLAIRE, WIS.    | Uniroyal Chemical Corp. |
| SOUTH BAY, FLA.     | U.S. Sugar Corp.        |
| KLAMATH FALLS, ORE. | Weyerhaeuser Co.        |

the new jobs will pay more than \$8 an hour, a far cry from the average of \$14 an hour at Uniroyal.

The single factor driving successful redevelopment: almost fanatical local leadership. Columbus, Ind., some 60 miles south of Indianapolis, watched 6,600 jobs disappear during the early 1980s when recession and foreign competition hit the town's biggest employers, Cummins Engine Co. and auto-parts maker Arvin Industries Inc. Columbus didn't die because Cummins' chief executive at the time, Henry B. Schacht, and Arvin's James K. Baker aggressively helped to market the town—which is nestled between two interstates—to companies looking for a location from which to supply the industrial heartland. Schacht even appointed a Cummins executive, Brooke Tuttle, to spearhead the effort.

Ten years later, Tuttle has managed to lure 28 companies, among them Toyota Industrial Equipment's forklift operation and 11 other businesses from Japan, and has created 6,580 jobs. Unemployment is under 4%, compared with 12.3% in 1983, and now Schacht is worried about a labor shortage. Even in Columbus, however, the new jobs pay just \$8 or \$9 an hour. Most Cummins workers get \$15. For old company towns, it seems, even the best news is a mixed blessing.

By Kevin Kelly in Columbus, Ind., with bureau reports

HOME IN INDIANA: TOYOTA WAS ONE OF 12 JAPANESE COMPANIES LURED TO COLUMBUS





ped address this shortcoming: A consortium of 21 area  
ks, for example, operates a loan pool for risky small busi-  
nesses that don't meet typical lending standards.

Meanwhile, the region has fostered entrepreneurship. Bob  
ter's incubator, one of several seeded by county and state  
ney, provides its tenants low-rent space—old IBM space—  
low rates on office services. Ritter hopes that, given  
or three years, his fledgling entrepreneurs will fill some  
of the region's empty real estate. Already, though, small  
business is sprouting throughout the area. Silicon Valley it's  
not. But absent IBM's security blanket, some people have be-  
come risk-takers. "I used to think my career was going to be  
at IBM, and I'd retire there someday having made all the mon-  
ey I needed," says Henry Duquette, 40. No more. Duquette  
works at IBM, building and repairing test equipment.  
On the side, he has started Duquette Limousine, hiring  
his two cars for \$40 an hour.

James Capralos has turned entrepreneur, too. After 29  
years with IBM in Poughkeepsie, Capralos took early retire-  
ment, at 52, from his \$70,000-plus systems analyst job. He  
did part-time maintenance work, then quit to open the  
theatre sales and distribution office for his brother-in-  
law's small prescription-drug-packaging company.

Today, Capralos' office is his living room. He is his only em-  
ployee. He makes a fraction of his IBM salary—and he loves it.  
"I never thought I would end up being a salesman," he says.  
"I don't know what I would have given two  
years ago that I'd be doing  
this." The words of a born-  
in Beemer.

Will the Valley make it?  
The numbers look remarkably  
good. Dutchess County's un-  
employment rate has slipped  
to 4.5%, the lowest since  
1980. Sales-tax collections, a  
measure of retail activity,  
upped 8.2% last year from  
1993. Wages, a key barometer  
of job quality, are coming  
back up.

Certainly, there is a trou-  
bling undercurrent. The re-  
gion's labor force has shrunk  
by 6% in two years, reflecting  
the exodus of thousands of  
IBM-led engineers and assem-  
bly workers—"a competitive  
edge that may already have  
disappeared," says Marist Col-  
lege economist Ann E. Da-

White officials say they  
are close to attracting as

many as three new high-skill employers, the county's  
biggest single recruit is the U.S. Postal Service,  
which will hire at least 800 semiskilled workers—  
most of them part-timers—to operate electronic im-  
age scanners. The state plans to fill half of IBM's empty King-  
ston plant with similarly low-paid data processing employees.  
Retail sales are strongest for the big discounters that now  
border a 10-mile section of Route 9, the county's commercial  
strip, and office space goes begging at \$4 to \$8 a square  
foot, roughly half what it was two years ago.

In the face of such challenges, however, signs of the Val-  
ley's rebirth are unmistakable. IBM is healthier than it has  
been in years, largely because of the strength of the Pough-  
keepsie-based mainframe unit. Local developers are building



# One of the new assets: A fresh cadre of civic leaders who remember the sins of the past

small office buildings and upscale homes again, and a Manhat-  
tan businessman has tentatively agreed to buy the other  
half of the Kingston plant. At the Poughkeepsie Chamber of  
Commerce, membership has doubled in four years, to 1,400.  
For every ex-Beemer still without work, it seems, there is a  
James Capralos.

The community is changing, subtly. Its dependable IBM  
audience gone, Poughkeepsie's Bardavon Opera House has  
broadened its repertory to appeal to new markets; a gay/les-  
bian opera came to town last spring. The shopping malls

along Route 9 have extend-  
ed their evening shopping  
hours to accommodate the  
swelling commuter population.  
At inner-city Poughkeepsie  
High School, 100% of this  
year's graduates will go on to  
college. Says Principal Theo-  
dore Peterson: "There's just  
not a hell of a lot of work  
here for these kids. Not any-  
more. They're better off get-  
ting into college as soon as  
possible."

**SLEEPY HOLLOW?** Those are  
good signs. The Hudson Val-  
ley is adapting, adjusting,  
preparing for a new way of  
life. It has woken up:  
Wrenching change will do  
that. Across the region, peo-  
ple are learning to take  
greater responsibility for  
their careers and lives, and  
to think of their communities  
in terms of collective self-  
determination.

The risk is that they'll fall  
asleep again, lulled back into  
complacency by the cushion created by commuter  
and retiree dollars. That isn't likely, however. If  
nothing else, there exists a cadre of civic leaders  
committed to remembering the many sins of the

past. "The mistake is in believing this place is superior to other  
places," says Charles E. Conklin, whose Conklin Instru-  
ment Corp. has operated in the Hudson Valley for 38 years.  
"It's not."

Not yet, anyway. But it soon could be. Fayiz Hilal, Richard  
Borstelmann, Kathleen Sullivan Norat, and many others are  
working on it. Their valley, now out from under Big Blue's  
shadow, is coming back.

By Keith H. Hammonds in Dutchess County, with Ira  
Sager in New York



**FED CORP.  
RUSHED NORTH  
TO GRAB PRIME  
EX-IBM SPACE**



## BASEBALL

# HITTING A GRAND SLAM IN A STRIKEOUT YEAR

Why the Colorado Rockies are keeping their stands full

In this summer of discontent for Major League Baseball, 8-year-old Aaron Bell seems an anomaly. Even as many former fans boycott the sport, Bell is doing everything he can to root his team, the Colorado Rockies, to a pennant. His bedroom in the Denver suburb of Englewood sports a Rockies bedspread, Rockies curtains, and walls plastered with photos of his favorite players and other memorabilia. And more often than not, Bell, a member of the Rockies' Rookies Kids Fan Club, is decked out in a team cap or T-shirt.

Baseball is in big trouble in most Major League cities. But not in Denver, where thousands of fans such as Aaron Bell are almost ecstatically embracing the game. As of Aug. 28, the Rockies have sold out 38 consecutive home games and should easily lead the majors in attendance this year, with a projected total of more than 3.4 million. Demand is so strong that "we're getting 5 to 10 times the face value for some tickets," says Patrick M. Chomyn, sales manager at Ticketman Inc., one of Denver's leading ticket brokers.

**LONG WAIT.** It's a Hall of Fame performance in a year when many clubs can't get to first base. Among all 28 teams, average attendance is running some 18% below last year's pace. It's also off 17% in Denver but only because the Rockies moved from 76,000-seat Mile High Stadium into their new home, Coors Field, which at 50,200 seats is 34% smaller. With TV ratings also in a slump, ABC and NBC recently announced they were pulling out of the Baseball Network, their deal to broadcast the sport. And with baseball's total revenues expected to plunge 30% to 40% this year—or up to \$800 million—"a record number of teams,

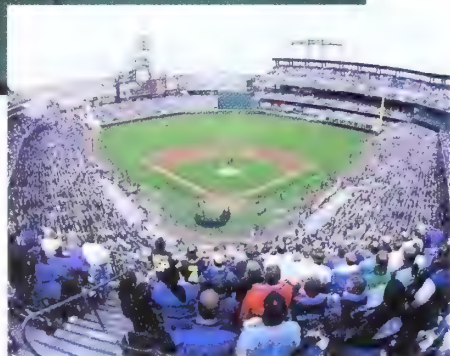
as many as 18, are losing money," says Andrew Zimbalist of Smith College, one of the nation's top baseball economists.

Things are so grim that only a handful of teams are bucking the trend—notably the Boston Red Sox and the



## FAN-FRIENDLY BALLPARK

Larry Walker hobbles with folks in packed Coors Field, where the beer is fresh: It's made right in the stadium



Cleveland Indians, a red-hot club that will draw at least 2.8 million fans, the most in its history. But no team can rival the Rockies, who are playing in one of baseball's smaller markets yet in just three seasons have shattered virtually every Major League attendance record.

Cynics are quick to note that the Rockies are benefiting from several special factors. Because this is just their third season, they're still in the honeymoon stage with fans in the Rocky Mountain states "who waited over 30 years for baseball to come to Denver,"

says Rockies CEO Jerry D. McMorris. Moreover, this is the Rockies' first year in Coors Field, a \$215 million gem that evokes the feel of an old-time ballpark. At the same time, it offers state-of-the-art concessions, including the first stadium microbrewery: the SandLot, which makes brews such as Squeaky Play Wheat and Slugger's SandLot Stout. On the field—thanks to the high altitude—more home runs are than in any other stadium. And the Rockies are in 1995's only real pennant race, with the Los Angeles Dodgers.

But such special edges hardly guarantee success. The Florida Marlins are also just three years old, the Texas Rangers are playing in a sparkling stadium that opened just last year, and the Atlanta Braves are the National League's best team. Yet attendance is way down those markets.

**BIG SPENDER.** So what made the difference in Denver? Much of the credit goes to owner McMorris. He made a fortune building NW Transport Service Inc. into the nation's largest privately owned trucking company, with revenues topping \$500 million. Now, McMorris is channeling his drive in the Rockies, where he employs his staff to put the

fans first. It shows. While other owners bemoan high payrolls, McMorris regularly throws money at Rockies fans, "making it possible for us" to acquire such high-priced talent as outfielder Larry Walker and pitching ace Brian Saberhagen. Yet even as the payroll

has soared to \$35 million from just \$15 million in 1993, McMorris insists on part of the park offering the cheapest seats in baseball. In "the Rockpile," a 2,300-seat section behind center field, a family of four can watch for as little as \$10.

McMorris is now vowing to win the World Series "faster than the Miracle Mets" of 1969, who clinched it in their team's eighth season. Whether or not he meets that goal, his Rockies have already given the rest of baseball plenty to think about.

By William C. Symonds in Denver



# BALTIMORE



MID-ATLANTIC'S TECHNOLOGY AND FINANCIAL HEADQUARTERS  
*for the 21st century*

"Baltimore will be to marine biotechnology  
what Cape Canaveral is to the space industry"

MAYOR KURT L. SCHMOKE



# BALTIMORE

MID-ATLANTIC'S TECHNOLOGY AND FINANCIAL HEADQUARTERS FOR THE 21ST CENTURY

Bell Atlantic was gearing up to develop the next generation of telecommunications technology: an interactive system offering customers multi-media services from



**SURVEYS CONSISTENTLY RANK THE JOHNS HOPKINS HOSPITAL AS THE NATION'S BEST.**

video-on-demand to home shopping. A half dozen cities were considered as the site for the 700 engineers who would collaborate in the network's creation. Baltimore quickly rose to the top of the list because of its central location, affordable office space, and pro-business attitude.

When Dr. Robert Gallo decided to leave the National Institutes of Health to start his own lab last year, cities across the country lined up to court the world-renowned AIDS researcher. But in the end the facilities at the University of

Maryland's Medical Biotechnology Center in Baltimore, the close connection with the University of Maryland Medical Center, and the strong support of city and state government won.

Sylvan Learning Systems, Inc. has experienced world-wide growth since moving its headquarters to the Baltimore area in 1991. Sylvan has grown from an after-school tutoring business into one of the world's leading providers of educational services to families, schools and industry. The company could have taken its approximately \$100 million in revenues elsewhere,

but chose to locate in the Empowerment Zone near Baltimore's famous waterfront. "We really see Baltimore as becoming the Silicon Valley for the education industry," says Sylvan's president Douglas Becker. "And the

Empowerment Zone is a powerful economic catalyst for businesses to move into the city."

During the past few years, Baltimore has emerged as the location of choice for entrepreneurs and blue-chip corporations in a wide range of high-technology industries, including communications, computer processing, biotechnology, and pharmaceuticals.

**BALTIMORE'S ENTREPRENEURIAL SPIRIT**  
Baltimore's ascendance as a technology center comes

as no surprise. Over the centuries the area has been a hotbed of entrepreneurial firsts, including the discovery of vitamin D and the synthetic sweetener saccharin by Johns Hopkins researchers, and the development of bufferin by University of Maryland Baltimore doctors.

Now Baltimore intends to be the first to catch the next wave of the technology revolution. The Columbus Center is the only organ-



**BRIGHTEN BALTIMORE, A CITY PARTNERSHIP WITH THE BALTIMORE GAS AND ELECTRIC COMPANY (BGE) TO PROMOTE DOWNTOWN VITALITY.**

ization in the U.S. aimed specifically at marine biotechnology research. At the 257,000-square-foot Center, 350 world-class researchers will focus on an entirely new niche of science whose applications for environmental engineering, for new pharmaceuticals, and for aquaculture are practically limitless.

**COVER: THE COLUMBUS CENTER - BALTIMORE'S WORLD CLASS INSTITUTION FOR MARINE BIOTECHNOLOGY RESEARCH AND EDUCATION.**

# "BGE has powered Baltimore's success for 179 years. That's a lot of experience to plug into."

- Chris Poindexter, Chairman and CEO

When Baltimore Gas and Electric installed the first indoor commercial gas lamp back in 1817, some people scoffed.

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# BALTIMORE

MID-ATLANTIC'S TECHNOLOGY AND FINANCIAL  
HEADQUARTERS FOR THE 21ST CENTURY



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**JOHNS HOPKINS**  
UNIVERSITY

Asserts Baltimore Mayor Kurt L. Schmoke: "Baltimore will be to marine biotechnology what Cape Canaveral is to the space industry."

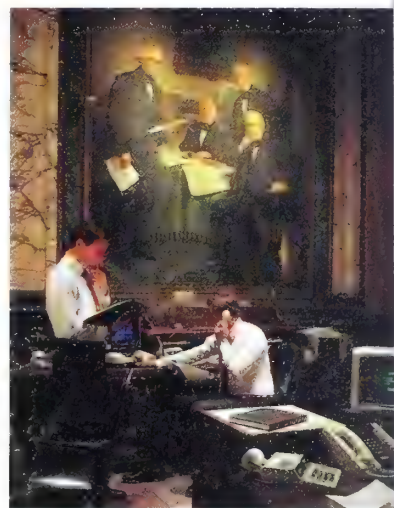
## UNMATCHED INTELLECTUAL TALENT

The City of Baltimore offers a number of powerful attractions to companies in the high-tech, bio-tech fields: an unusual concentration of top-flight research scientists and institutions; proximity to Washington, D.C., the source of federal funding and the seat of regulatory power; strong backing by financial institutions and venture capitalists; and a city and state government committed to making the Baltimore region a leader in technology research and commercialization.

Some of the most talented scientists in the world are hard at work in Baltimore, unlocking the secrets of the AIDS virus, creating new vaccines for dreaded diseases, and opening the door to the next generation of interactive communications technology. Feeding this rich pool of intellectual capital are the area's research universities.

The Johns Hopkins University wins more federal research dollars annually than any other American college or university—\$804 million in 1994 alone. The University of Maryland at Baltimore (UMAB) is the fourth fastest-growing research university in the country and is the site of the nation's

oldest teaching hospital. The University of Maryland Medical Center is known for cutting edge research and the latest patient care technology, including a Gamma Knife and stem cell transplants for cancer patients.



**ALEX. BROWN & SONS IS THE OLDEST INVESTMENT BANKING FIRM IN THE COUNTRY AND THE NUMBER ONE FINANCIER OF HIGH-TECHNOLOGY AND BIO-TECH VENTURES WORLD-WIDE.**

And at the young and entrepreneurial University of Maryland Baltimore County (UMBC), funding for research grants has skyrocketed from \$3.5 million in 1986 to over \$30 million today.

Through aggressive technology transfer initiatives, the universities make sure the relationship between scientists and business people works.

In 1994, discoveries and inventions made at Johns Hopkins were awarded 33 patents and 66 license and options. UMAB has received 350 invention disclosures since its inception in 1989, a thirteen-fold

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# BALTIMORE

MID-ATLANTIC'S TECHNOLOGY AND FINANCIAL HEADQUARTERS FOR THE 21ST CENTURY



**NUMEROUS HIGH-TECH AND BIO-TECH FIRMS HAVE CLUSTERED AROUND BALTIMORE TO TAKE ADVANTAGE OF THE AREA'S INTELLECTUAL TALENT AND GROWING SUPPLY OF VENTURE CAPITAL.**

increase over the previous five years. "We see ourselves as marriage brokers," says Joann Boughman with UMAB's Office of Technology Development.

"We want to get the faculty person with the idea together with the money person. But they have to trust each other before the relationship will work."

**F**ROM THE BENCH TO THE MARKETPLACE Baltimore's rich repository of research talent has already yielded gold in the way of business success stories. Dr. Solomon Snyder's discoveries in neuroscience at Johns Hopkins enabled him to spin off Nova Pharmaceuticals in the 80s and Guilford Pharmaceuticals in the 90s. At Guilford, a treatment

for brain cancer nears the end of its clinical trials. Johns Hopkins' scientists have started seven companies: UMAB researchers, five.

The next wave of entrepreneurial success stories may include companies like CardioLogic. Founded by physicians from Johns Hopkins, the company is test marketing a "vest" that wraps around a heart attack victim's chest and automatically performs CPR. At UMAB, scientists have developed a new vaccine for cholera which will soon be used across the world to prevent the deadly disease. An oxygen sensor

## LEADERS IN BIOTECHNOLOGY

Maryland's leading educator of professionals, the University of Maryland at Baltimore (UMAB) is home to schools of medicine, dentistry, pharmacy, nursing, law, social work and graduate studies.

The university is one of America's fastest growing biomedical research centers, with special strengths in vaccine development, neuroscience, pharmaceuticals, geriatrics, health policy and toxicology. UMAB faculty collaborate interprofessionally to design and evaluate new practice models for delivering health care, social welfare and legal services.

New facilities for health sciences research and medical biotechnology come on line this year. Annual grant and contract funding exceeds \$110 million. Energetic, entrepreneurial leaders support UMAB's spirit of academic innovation and its goal of bringing new technologies to the



marketplace. For more information call Technology Development, (410) 706-1874.

In the heart of the UMAB campus stands America's oldest teaching hospital — the University of Maryland Medical Center. It is known for excellence in cancer care, neurocare, transplant surgery, cardiac care, women's and children's health, trauma care and rehabilita-

tion services. Equipped with the latest technology and an outstanding staff, the Medical Center:

- › Trains almost half of Maryland's practicing physicians and health care professionals
  - › Has one of the largest organ transplant surgery programs on the East Coast
  - › Has the only Gamma Knife in Maryland, used to destroy brain tumors without surgery
  - › Is home to the R. Adams Cowley Shock Trauma Center, the nation's first and largest trauma facility
- The Medical Center, Baltimore's sixth largest employer, is located just three blocks from the new Oriole Park at Camden Yards in downtown Baltimore.



**UNIVERSITY OF MARYLAND  
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SPECIAL ADVERTISING SECTION

# BALTIMORE

MID-ATLANTIC'S TECHNOLOGY AND FINANCE  
HEADQUARTERS FOR THE 21ST CENTURY

instrument created by engineers in a UMBC "incubator" is bound for the pharmaceutical marketplace, backed by the bio-tech giant, Genentech.

**FLEXING ITS FINANCIAL MUSCLES** Technology start-ups as well as mature companies require careful financial management to make it through the often years-long research and testing phase. Baltimore offers businesses a vigorous mix of financial options from conventional banking, to venture capital to innovative public/private collaborations.

Baltimore is home to some of the most prestigious names in American finance — Alex. Brown & Sons, T. Rowe Price, Legg Mason, Fidelity and Deposit, and USF&G. The number one underwriter of venture-backed IPOs for eight years running, Alex. Brown in the past two years has managed 50 technology-related financings that raised over \$2.5 billion. The company's credentials include taking Microsoft public 10 years

"It's highly unusual that the leading firm in high-tech and bio-tech financing is right here in Baltimore at a time when the city and business community are focusing their energies in that direction," says Mayo Shattuck, III, president and COO of Alex. Brown.

The number of venture-backed IPO's has jumped dramatically during the past four years as the venture community has increasingly become aware of investment opportunities within the region. According to a Price Waterhouse research group, the region led the nation in venture capital investments during the first three months of 1995 with 19.1 percent of the total. Between 1992 and 1994, venture firms raised more than \$500 million for 92 companies in the Baltimore-Washington region, including the District of Columbia and Northern Virginia.

Says Charles Newhall, president of the Baltimore venture capital firm, New Enterprise Associates: "Baltimore has gone from nowhere to being a major factor in key new technologies. There are about 500 venture-backed high-tech firms in the region now."

Commercial banks are finding new ways to invest



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TAKING OWNERSHIP



# BALTIMORE

MID-ATLANTIC'S TECHNOLOGY AND FINANCIAL HEADQUARTERS FOR THE 21ST CENTURY

high-risk technology companies with a little help from the state. Last year, Signet Bank agreed to buy \$8 million in bonds for Guilford Pharmaceuticals after the state provided a \$3.4 million guarantee. NationsBank got a similar guarantee—\$3 million—for its \$5 million loan to Genetic Therapy, Inc.

"The city has a long history of being an active player in stimulating business development," says John Weiss, managing partner of Anthem Capital, a new venture capital firm with a regional focus. Baltimore City has invested \$1 million in the firm, which as a small business investment corpora-

More than thirty years ago, Baltimore began one of the most ambitious programs of urban renewal ever devised. The city's Inner Harbor—240 acres of scenic waterfront—won over three dozen international awards for excellence in urban design and architecture. More recently, city and state government officials and local business leaders pulled together to build the celebrated Oriole Park at Camden Yards.

"The business community is really joined at the hip when it comes to getting single projects done," says Shattuck of Alex. Brown. "I can't think of another city where people rally together in such a unified way."

Similarly, the Columbus Center was developed with \$160 million in federal, state, city, and private funds and is one part of a significant build-up of high-tech facilities in Baltimore. In the

next few years hundreds of thousands of square feet of state-of-the-art research facilities will have come on-line in Baltimore, including a proposed 95-acre research park at UMBC, the Maryland BioCenter, a manufacturing facility for bio-tech companies, and the Alpha Center, an incubator lab for start-up companies, both part of the development at Johns Hopkins Bayview Research Campus.

## BALTIMORE: A LAUNCHING PAD TO INTERNATIONAL MARKETS

From its colonial heritage, Baltimore has been a major center for international commerce. World Trade magazine ranked Baltimore among America's 10 best cities for international companies.

One strong draw is the Port of Baltimore, the second busiest port on the Eastern seaboard. Its location 200 miles inland puts it just an overnight truck ride away from 32 percent of the U.S. population and 34 percent of its manufacturing base. The Baltimore-based Terminal Corporation has joined with a Canadian stevedoring company to create a system for electronic data transfer with international customers and bar code data collection for cargoes moving through the terminal.

The Port connects with a sophisticated transportation network linked by 22,000 miles of public roads and a burgeoning international airport within minutes of downtown Baltimore. During the first four months of 1995, international traffic through Baltimore-Washington International (BWI) Airport had risen 18.3 percent over the previous year.

**THE WORKFORCE: TRAINED FOR HIGH-TECH JOBS** Using the slogan "Baltimore. The City That Reads," Mayor Schmoke



THE HIGH-TECH CAPABILITIES AND STRATEGIC INLAND LOCATION OF THE PORT OF BALTIMORE HAVE ATTRACTED FIRMS INTERESTED IN MAKING A SPLASH IN THE INTERNATIONAL MARKETPLACE.

tion gets \$2 of equity investment through the Small Business Administration for every \$1 raised.

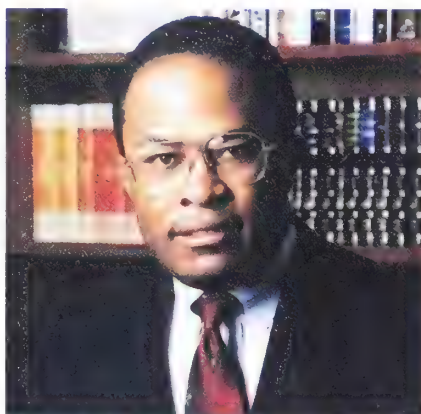
Baltimore has focused political will and financial resources into becoming a high-tech, bio-tech powerhouse on the East Coast. If the past is predictive, the city will succeed.

# BALTIMORE

MD-ATLANTIC'S TECHNOLOGY AND FINANCIAL HEADQUARTERS FOR THE 21ST CENTURY

omoting a city-wide campaign insure that tomorrow's workers are not only literate but have the skills needed in a high-tech workplace. Toward that end, Baltimore offers free access to the Internet through its public library system. Recently the city joined with Bell Atlantic to connect area high schools to Distance Learning—full-motion interactive video network. Bell Atlantic is donating classroom equipment for every participating school—a contribution of up to \$13 million.

"We're committed to getting



MAYOR KURT L. SCHMOKE

young people involved at the earliest possible age with interactive computer technology," says Mayor Schmoke. "Distance Learning allows

us to move information to where the learners are. It could change the way we view public education."

The city's commitment to the workforce of the future can be seen at the Columbus Center where a science and technology education center brings area school children in direct contact with real scientists and their discoveries. "We are bringing science right into the city," says Dr. Rita Colwell, president of the University of Maryland's Biotechnology Institute of which the Columbus Center is a part. "The Center makes science and

## A completely objective guide to relocating your business.

[Compliments of Maryland - the absolute, without a doubt, by far, best state for your business]

### 1. Make sure it's convenient to transportation.

The state you choose should be located near major transportation like, for example, Maryland which is located right in the middle of the Eastern Seaboard with I-95, the Port of Baltimore, BWI Airport, and the CSX Rail System.

### 2. Check out the work force.

Make sure the state offers a well educated, stable work force like, for example, Maryland where workers with bachelors degrees exceed the national average by 19.2%.

### 3. See what other businesses are located there.

Make sure different types of businesses have had success in the state like, for example, Maryland where companies

like Westinghouse, Black & Decker, USF&G, Legg Mason, Lockheed Martin and Procter & Gamble are doing very well.

### 4. Make sure you'd want to live there.

Check to see that the state has good educational and health care facilities like, for example, Maryland which has Johns Hopkins and the University of Maryland, each with its own renowned medical facility.

To find out more about what a great place Maryland could be for your business, contact Victor Hoskins at (410)333-6989, or fax your request to the Division of Marketing, Maryland Department of Business and Economic Development, (410)333-6608.

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# BALTIMORE

D-ATLANTIC'S TECHNOLOGY AND FINANCIAL HEADQUARTERS FOR THE 21ST CENTURY

search part of our daily lives in meaningful way."

"At UMBC' innovative partnerships with high-tech businesses are helping usher talented students into challenging, high skilled jobs. Says UMBC' resident Freeman Hrabowski, "Companies coming to the area often ask whether they'll be able to find a ready supply of technicians. We have hundreds of students and want to give young people the opportunity to work in the real world of business early in their careers."

Zones are nurturing small businesses and revitalizing neighborhoods. The "Brighten Baltimore" campaign



THE PRIDE OF BALTIMORE IS A REPLICA OF THE SPEEDY TOPSAIL SCHOONERS CREATED IN THE EIGHTEENTH CENTURY WHEN BALTIMORE LED THE NATION IN SHIPBUILDING. TODAY, THE SHIP DOCKS AT THE INNER HARBOR AND PLAYS HOST TO NUMEROUS CIVIC AND BUSINESS GATHERINGS

with Baltimore Gas and Electric Company is lighting up city streets. A new children's museum, called Port Discovery, being developed by Walt Disney Imagineering and the Rouse Company, will join the Columbus Center and the National Aquarium as favorite destinations for family education and entertainment.

"We want every citizen to be part of our city's success story," says Mayor Schmoke. "The renaissance of Baltimore will not be complete until all have an opportunity to share in it."

**A BIG CITY, SMALL TOWN SENSIBILITIES** Baltimore boasts a lower cost of living than other comparable cities. Employees who work long hours enjoy the fact that they can leave the office and get home or to the airport in fifteen minutes.

After hours, residents enjoy the uptown sophistication of the world-class Baltimore Symphony Orchestra, the famous Walters Art Gallery, the Baltimore Museum of Art, and the Lyric Opera House. From active participants to armchair enthusiasts, the sports-minded have it all, in particular the Baltimore Orioles, Baltimore CFL allions, and an array of water activities on and around the magnificent Chesapeake Bay.

Further enhancing the city's quality of life ranks high on the mayor's agenda: Empowerment

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SYLVAN LEARNING SYSTEMS



EDITED BY JIM ELLIS

## AN ARSENAL OF NEW WEAPONS AGAINST STROKE

**F**or years, there was little urgency in the treatment of stroke—often caused when a clogged artery chokes off blood flow to part of the brain—because it was believed there wasn't much doctors could do. Ambulance drivers picked up heart attack and stab-wound victims first, then the stroke cases. "Physicians used to be taught this was the way patients like grandma were supposed to die," says neurosurgeon Michael Walker, a director of the National Institute of Neurological Disorders & Stroke (NINDS).

Now, all that is changing. Better preventive therapies and education are heading off many strokes before they strike. And once they occur, doctors are starting to think of strokes in more dramatic terms: a brain attack to be treated as an emergency. This major change in thinking is taking shape because clot-busting drugs, intriguing neuroprotective agents that guard against the brain-cell death that robs victims of mobility, speech, or memory, and advanced surgical techniques are improving the outlook for survivors.

"It's the most exciting time in the history of stroke treatment," says Gary Houser, vice-president of the National Stroke Assn. "We are on the threshold of having a true treatment that can be used after the onset of symptoms."

Big numbers are driving the surge of interest in stroke treatments. More than

550,000 people have a stroke each year in the U.S., making it the third-leading cause of death. Of those half-million victims, 150,000 die. The remaining 400,000 endure handicaps, making stroke the chief cause of disability. These numbers are expected to increase as boomers age.

What are the chances you might become an unlucky statistic? Topping the list of risk factors are high blood pres-

sure, high cholesterol, family stroke history, taking high-dose estrogen oral contraceptives, heart disease, diabetes, smoking, consuming more than two drinks of alcohol daily, using illicit drugs such as cocaine, and being more than 30% over your optimum weight. Stroke doesn't happen only to the elderly, either: About 28% of all stroke victims are under 65.

More worrisome than risk

factors are warning signs. These include temporary numbness, weakness, or paralysis of the face or limbs, especially on one side. Other hints of trouble are loss of balance, sudden blurred or decreased vision, difficulty speaking or understanding simple statements, and sudden severe headache for no apparent reason. Some of these incidents, known as transient ischemic attacks (TIA), may pass within a few moments. But physicians recommend a trip to the emergency room. Don't wait until Monday morning to call your internist. If it happens, it's impossible to tell whether it's a TIA or a stroke. Quick action is essential, because researchers have discovered that there is a critical six-hour window of time after stroke during which newly developed treatments can halt or reduce death. "Beyond that, the damage to the imperiled or injured brain is irreversible," says Houser.

**CLOT-BUSTERS.** Once a stroke hits, brain cells begin to die and release chemicals that set off a chain reaction endangering cells in the surrounding area called the penumbra, where the blood supply may have been reduced but not cut off. Without emergency treatment, the larger area of cells will also die. But many hospitals are now experimenting with two types of compounds that, if administered quickly, may dissolve clots or protect cells from imminent destruction. The clot-busters, such as

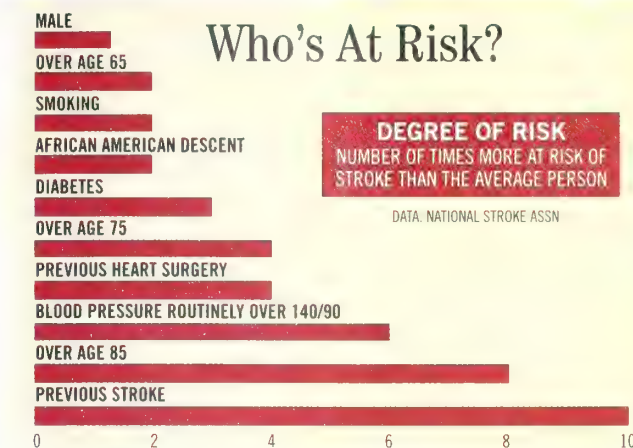


**HEALTH**



entech's tissue plasminogen activator (TPA), have the potential to revolutionize treatment by restoring blood flow before massive damage is done. Although already used for heart attacks, TPA remains controversial for stroke because it can cause serious bleeding. Neurologist Gregory W. Albers, director of the Stroke Center at Stanford University Medical Center, is participating in a study of 200 patients who receive TPA within five hours of their stroke symptoms. Because it is a double-blind study, Albers doesn't know which patients get TPA and which receive placebos but recover spontaneously. Nevertheless, he remains hopeful: "We've had a number of patients whose strokes have disappeared within 6 to 12 hours after treatment."

Another class of compounds, called neuroprotective agents, can shield irreplaceable brain cells by blocking the deadly advance of calcium that occurs when glutamate levels rise during a stroke. Other protectants, called azaroids, include com-



can use them before a stroke hits. Last fall, the results of a study on carotid endarterectomy, the removal of fatty deposits from the neck artery that carries blood to the brain, were so compelling that NINDS cut short its \$20 million study. It recommended considering surgery even for patients with no symptoms—but who had a 60% or more narrowing of the carotid artery. Based on a trial of 1,662 men and women between the ages of 40 and 79, the study showed that the risk of stroke was reduced

make the operation safer," says Wesley Moore, chief of vascular surgery at the University of California at Los Angeles. NINDS recommends using only a surgeon whose complication rate (death or stroke during surgery) is less than 3%.

But if you experience no symptoms, how do you know what shape your neck arteries are in? Simply ask your physician to listen to your neck with a stethoscope during your next checkup. The detection of a swishing sound should prompt your doctor

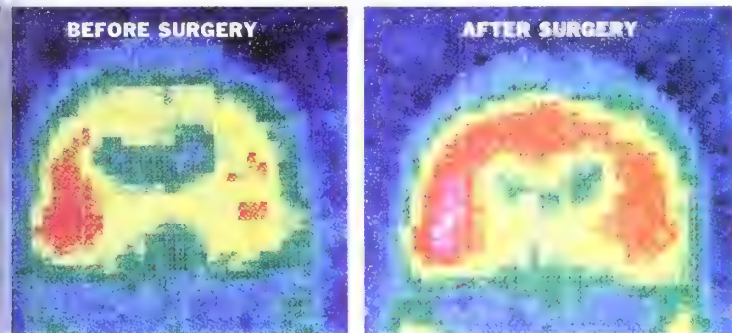
to order an ultrasound and other tests to measure any possible narrowing. Also important: Check out either vascular surgeons or neurosurgeons who have 50 or more carotid endarterectomies under their belts. If surgeons merely quote the medical literature and can't

cite their own statistics, they may not be doing enough surgeries to be skilled in the delicate task of removing the blockages without breaking off some and inducing a stroke. Experts say it's best to go to a center where large numbers of the procedure are done, such as New York's Columbia-Presbyterian Neurological Institute or Barrow Neurological Institute in Phoenix.

Interventional neuroradiol-

ogists are also pioneering less invasive, nonsurgical techniques for brain rescue. To repair an aneurysm, a bulb-like weakening in the wall deep inside the brain, before it bursts—a feat unthinkable 10 years ago—physicians today use sophisticated imaging technology that lets them guide tiny platinum coils through a groin artery up to the brain. The coils are pushed into the aneurysm, which then clots off. Angioplasty, in which a small balloon in the arteries opens narrowed vessels, is also making its way from the heart to the neck and brain. It is sometimes used with TPA, which is injected directly into the narrowed site.

Remember that lifestyle changes such as a healthier diet and exercise help decrease your chances of a stroke, and a host of common medications can reduce blood pressure, thin the blood, and prevent clots. So while there's still no single cure for stroke, people with risk factors are no longer fated to succumb to this common and cruel affliction. *Barbara Buell*



**MAIN SCAN:** Blood flow (in red) is restored to a stroke victim

unds such as Upjohn's tirilid, which helps prevent cell breakdown during stroke. While these agents may lessen the damage in the early hours after stroke, their efficacy is still unproved. Albers says: "It will be at least five years before these are in everyone's hospital armory."

Meanwhile, advances in surgery and interventional neuroradiology are now astonishingly effective—and you

by 55% in patients who had the elective surgery.

**SPECIALIST CHECK.** Carotid endarterectomy has been performed since the '50s on patients with severe blockages. In the '80s, surgeons came under scrutiny for doing too many of these risky surgeries. But better patient selection and advances in diagnostics, anesthesia, and surgery have lowered the risks. "There have been a lot of technical improvements to

## Where to Find Out More

**NATIONAL INSTITUTE OF NEUROLOGICAL DISORDERS & STROKE**  
Office of Scientific & Health Reports  
Building 31, Room 8A-06  
31 Center Drive MSC-2540  
Bethesda, Md.  
20892-2540,  
800 352-9424

**THE NATIONAL STROKE ASSN.**  
8480 East Orchard Road,  
Suite 1000, Englewood,  
Colo. 80111-5015,  
800 STROKES

**AMERICAN HEART ASSN.**  
7272 Greenville Ave.  
Dallas, Tex. 75231  
800 242-8721 (prevention and treatment)  
800-553-6321 (survivors and families)

DATA: BUSINESS WEEK





## A PERSONAL SHOPPER FOR YOUR DREAM HOUSE

When Sallye and Jim Ryan wanted to move from their Tampa apartment to a three-

bedroom home this spring, the busy couple used a buyer broker, Beth Tansey, to help. Within a week, they had bid on the house they now own. Sallye liked being able to delegate the house-hunting. "With both my husband and me working, it was a lot easier," she says. "I don't think I would have found this house that I really love without her. There are so many homes for sale here, I would probably still be looking."

Because Tansey is a buyer broker, who exclusively represents the home buyer's interests, the Ryans trusted her to find the best deal on a house that suited their needs. By contrast, a traditional real estate broker is legally bound to work for the seller who pays the commission and therefore may be more intent on selling listed homes than finding your dream house. Even realtors who don't hold the listing on a given house act as subagents to the seller. So unless a broker says that

he or she is working for you—brokers are now legally obliged to disclose who they represent—you can assume the broker is working for the seller. Such agents must pass on information such as the buyer's income to the seller, who then has a better idea of what price to hold out for.

But the balance of power in real estate transactions is changing as the number of brokers who serve only buyers grows. The two biggest national franchises are Buyers' Agent (800 766-8728), based in Memphis, and Buyers' Resource (800 359-4092), in Englewood, Colo. Both companies provide referrals to their own brokers as well

as independent buyer brokers across the country. Proof is still scant that buyer brokers are a boon. Some traditional brokers think they add little to the equation. "Basically, even though traditional agents have a fiduciary duty toward the seller, their priority is accomplishing the deal," says Dave Goldsmith, director of marketing at D.G. Neary, a New York real estate firm. "I don't know if it will change things except in people's minds."

**BEST DEAL.** However, there's reason to believe buyer brokers can save time and money. An informal survey by long-distance company Sprint in 1991 showed that employees who used buyer brokers saved an average of 9% off the asking price, vs. 3% for all home buyers. In addition, buyer brokers check into property values and school systems. "We make clients fully aware of areas that are appreciating, so they tend to buy in areas on the upswing," says Buyers' Agent President Tom Hathaway.

Because these brokers are obliged to get buyers the best deal possible, they approach houses with a critical eye for apparent flaws. You'll still need an inspector to uncover hidden defects, however. Buyer brokers also show properties sold by the owner, which can be cheaper because the only commission is what you agree to pay your broker. Sellers' agents usually won't show these homes because they don't make commissions on them.

## Who Represents Whom?

**EXCLUSIVE BUYER BROKER** Aims to get best deal for home buyer. Splits commission with seller's agent.

**TRADITIONAL REAL ESTATE AGENT** Represents the seller and is legally obligated to disclose personal information about the buyer, such as income, that could affect the sale price. Seller pays commission, which is built into the price of the home.

**DUAL AGENT** Works for a listing agency, which works for the seller, but is assigned as broker to the buyer. May push homes listed with agency.

DATA BUSINESS WEEK

Brokers representing buyers should also appraise the value of the house, negotiate the price, and prequalify you for a mortgage, sometimes at a better rate. Buyers' Agent brokers, for instance, narrow mortgage bids from 15 lenders nationwide to the three best offers—and then invite those three to rebid. "A well-trained, experienced buyer broker is a great asset," says Peter Miller, author of *How to Sell Your Home in Any Market* (\$12, HarperPerennial) and other real estate guides. "You won't do any worse, and you may do a lot better."

Usually, the buyer broker splits the sales commission with the seller's agent, just as a subagent who didn't have the listing would with the broker who did. So the fee still comes out of the sale price. Some people might assume that buyers' agents have an incentive to keep the price high. But again, the broker must get you the best deal. "In my experience, almost all of them do," says Stephen Brobeck, executive director of the Consumers Federation of America.

**STRAIGHT TALK.** A conflict of interest is more likely when a real estate firm that represents sellers assigns you one of its brokers as a buyer agent. That's why many people believe an "exclusive" buyer broker is preferable if there aren't any in your area, and you have to use a listing broker, "make sure they disclose when they are showing you properties they have a financial interest in," says Brobeck.

Unlike using a conventional realtor, you must sign an agreement to work solely with a buyer broker for a certain period of time. Don't sign up for more than three months, says Brobeck. That way, you know the broker must go all out for you rather than sit on your case for a few months. When your contract is up, you can renegotiate, find another agent, or go it alone. *Pam Black*



You could make rubber band balls for instance.

Or little paper clip figurines. But why on earth would you want to spend more time getting less done at work? Well, the answer is you probably wouldn't. No, one would. It's just that some people may not know that you can run Windows NT™ applications up to *three times faster* with a MIPS™ RISC-based system\*. Or that you can also use MIPS RISC with UNIX. And that according to the TPC-C benchmarks, the *top three OLTP systems* use MIPS RISC. On the other hand, it may be that these people *do* know about all these things, and have just had trouble convincing other people. So if you find yourself in this position, and you think it might help, you could always tell them that you chose

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works. But if not – if after all that, they

still seem unsure – just remember that you

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always be plenty of office supplies.

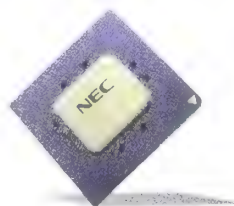
*You could run*

*Windows NT without*

*MIPS, but there are more*

*imaginative ways*

*of wasting time.*



**NEC**



\*Compared to a Pentium processor on a 486 system.

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## CAN'T AFFORD A LEAR? BUY A PIECE OF ONE

The flight from Tampa to Newark, N. J., should have been a cinch. Commercial realtor John Amend and his staff had finished one key meeting and were planning on an easy trip that left them plenty of time for getting to another the following day. But when can commercial business travelers count on things going perfectly?

Amend's American Airlines flight was sidetracked for hours by foul weather along the East Coast and a jet mishap in New York. Eventually, the plane was rerouted through Nashville and sent on to Newark. But by then it was 3:30 a.m., and a meeting with AT&T officials loomed less than five hours away. "We were tired, exhausted," recalls the 46-year-old president of Dallas-based Amend Group, a real estate consultant. "Delays like this had become routine."

So Amend decided to make sure he wouldn't again be stuck on the tarmac: He bought his own jet. Well, at least part of one. In a move that many executives of small- and medium-size businesses would have thought impossible just a few years ago, Amend purchased a stake in a LearJet 60 from Bombardier Business JetSolutions, a three-month-old venture between AMR Combs, an American Airlines subsidiary, and Canadian aircraft maker Bombardier.

Through JetSolutions' FlexJet plan aimed at smaller businesses, would-be owners most commonly buy an eighth or a quarter share of Bombardier-made business jets, which are then maintained by AMR Combs. Owners also have access to Combs's 13 corporate aviation service centers across the U.S. and Mexico. "We'd had enough of chartering and booking through commercial airlines," Amend says.

**GOODBYE STANDBY.** Per flight hour, FlexJet owners pay more than most other jet charter and fractional ownership schemes. But they don't pay for the time it takes their plane to reach them for pickup, nor for the time it

ers are entitled to 100 hours flying time per year, while one-quarter share owners get 200. But part-owners can book time on any of the three jet models in the fleet. So, a

airplanes, allowing them to take a depreciation expense.

Of course, with purchase prices between \$700,000 and \$4.7 million, hefty monthly fees of at least \$7,500, and

hourly charges as high as \$2,000, the FlexJet program isn't for everyone.

For instance, ownership shares expire after five years. And companies that use aircraft more than 100 hours a year may find sole ownership of a used aircraft more economical. Chartering a plane that's owned and managed by someone else, or starting a flight department, may be cheaper. And while 100% aircraft owners who are flying privately are exempt from the 10% federal excise tax, tax treatment of fractional owners is a murky area currently under litigation.

**NO-FRILLS.** For businesses that would rather not deal with a manufacturer or seek longer-term ownership, another option is a nine-year-old program called NetJet offered by Executive Jet Aviation based in Montvale, N.J. With Executive Jet, businesses do not buy the planes directly from the manufacturer; instead, EJA buys new planes and resells shares to fractional owners. But EJA does not have direct partnerships, as JetSolutions does, with a network of fixed-base operators who provide plush conference rooms, computers, and fax machines right at airports for business travelers. Adds Gilbert T. Wolin, an aviation management consultant based in Lafayette, Colo., "Sometimes it's more cost effective to buy a used aircraft and have it maintained by a locally based operator."

Whether they own or lease, a growing number of executives these days believe that having their own plane—rather than booking flights aboard commercial airlines—is really the best flight plan. *Christina Del Vecchio*



part-owner of a seven-seater LearJet 31A, which flies short hops of up to three hours, can also book time on a widebody Challenger—which seats 10 passengers and can fly from the U.S. to Europe—by trading a chunk of hours.

JetSolutions also lines up Federal Aviation Administration-certified pilots. Each plane in the fleet is outfitted with sophisticated radar and collision avoidance systems. "We wanted to make business jets more accessible," says Robert D. Gillespie, president of Business JetSolutions. And through FlexJet, an owner avoids the cost and headache of

establishing a corporate flight department, with its own maintenance staff and pilots. Such considerations often stop smaller businesses from buying aircraft. There are tax advantages, too. Owners have an undivided interest in their

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takes the plane to return to its home base after dropping off part-owners.

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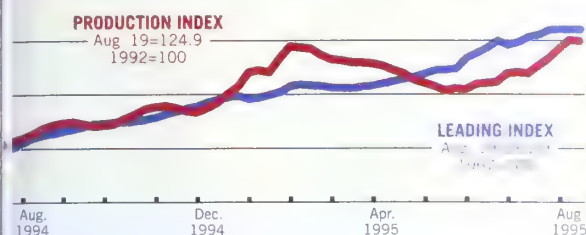
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## PRODUCTION AND LEADING INDEXES

Change from last week: -0.1%  
Change from last year: 5.2%

Change from last week: 0.0%  
Change from last year: 8.1%



**production index** was little changed in the week ended Aug. 19. Before calculation of the four-week moving average, the index rose to 124.6, from 123.8. Increases in the seasonally adjusted output of electric power, trucks, lumber, and rail-freight traffic offset declines in auto and steel production.

**leading index** was nearly unchanged in the latest week. The unaveraged index fell slightly, to 261.5 from 261.6. All of the major components moved up in the week.

production index copyright 1995 by The McGraw-Hill Companies. BW leading index copyright 1995 by The McGraw-Hill Companies.

## LEADING INDICATORS

|                                           | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|-------------------------------------------|-------------|------------|--------------|
| <b>STOCK PRICES</b> (8/25) S&P 500        | 558.47      | 559.31     | 19.4         |
| <b>CORPORATE BOND YIELD, Aaa</b> (8/25)   | 7.60%       | 7.64%      | -6.5         |
| <b>INDUSTRIAL MATERIALS PRICES</b> (8/25) | 114.9       | 113.8      | NA*          |
| <b>BUSINESS FAILURES</b> (8/18)           | NA          | NA         | NA           |
| <b>REAL ESTATE LOANS</b> (8/16) billions  | \$493.5     | \$492.8r   | 11.9         |
| <b>NEW SUPPLY, M2</b> (8/14) billions     | \$3,699.3   | \$3,695.9r | 3.4          |
| <b>UNEMPLOYMENT CLAIMS</b> (8/12) thous.  | 338         | 332        | 4.0          |

**Sources:** Center for International Business Cycle Research (CIBCR), Standard & Poor's, Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures large companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans. \*Historical data available from CIBCR

## INTEREST RATES

|                                               | LATEST WEEK | WEEK AGO | YEAR AGO |
|-----------------------------------------------|-------------|----------|----------|
| <b>FEDERAL FUNDS</b> (8/29)                   | 5.48%       | 5.68%    | 4.72%    |
| <b>COMMERCIAL PAPER</b> (8/29) 3-month        | 5.80        | 5.83     | 4.90     |
| <b>CERTIFICATES OF DEPOSIT</b> (8/30) 3-month | 5.76        | 5.78     | 4.88     |
| <b>FIXED MORTGAGE</b> (8/25) 30-year          | 8.10        | 8.20     | 8.70     |
| <b>ADJUSTABLE MORTGAGE</b> (8/25) one-year    | 5.92        | 6.05     | 5.61     |
| <b>LIBOR</b> (8/30)                           | 8.75        | 8.75     | 7.75     |

**Sources:** Federal Reserve, HSH Associates, Reuters Holdings PLC

Index data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### VEHICLE SALES

**Tuesday, Sept. 6** ▶ Sales of domestic-made cars and light trucks probably peaked at an annual rate of 12.3 million in August, according to the median forecast of economists surveyed by MMS International, of the McGraw-Hill Cos. Although some manufacturers will disclose their sales earlier, most others, including Ford Motor Co., report on Sept. 6. The expected August sales pace would be a rebound after the industry's steady decline in vehicle purchases. In July, sales fell a steep 6.3%, to a pace just 11.9 million, even though many carmakers offered rebates and other incentives. The sales downtrend lifted auto

inventories and caused a drop in production, which has accounted for two-thirds of the drop in factory output since March.

### UNEMPLOYMENT CLAIMS

**Thursday, Sept. 7, 8:30 a.m.** ▶ New filings for state unemployment benefits during the week ended Sept. 2 will probably fall to about 310,000. Claims had picked up in July, going above 400,000 in the second week. The rise partly reflected auto-plant shutdowns, which pushed up filings in that month. But jobless claims have fallen back since then, with only 348,000 in the week ended Aug. 19. Still, claims remain at a high level, given the tightness of the labor markets.

## PRODUCTION INDICATORS

|                                                       | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|-------------------------------------------------------|-------------|-----------|--------------|
| <b>STEEL</b> (8/26) thous. of net tons                | 1,904       | 1,873#    | 2.9          |
| <b>AUTOS</b> (8/26) units                             | 113,526     | 97,391r#  | -1.9         |
| <b>TRUCKS</b> (8/26) units                            | 113,587     | 109,374r# | -1.7         |
| <b>ELECTRIC POWER</b> (8/26) millions of kilowatt-hrs | 73,896      | 79,332#   | 9.9          |
| <b>CRUDE-OIL REFINING</b> (8/26) thous. of bbl./day   | 14,183      | 14,157#   | -1.6         |
| <b>COAL</b> (8/19) thous. of net tons                 | 19,873#     | 19,853    | -2.8         |
| <b>PAPERBOARD</b> (8/19) thous. of tons               | 883.2#      | 892.8r    | 0.5          |
| <b>PAPER</b> (8/19) thous. of tons                    | 835.0#      | 849.0r    | -1.6         |
| <b>LUMBER</b> (8/19) millions of ft.                  | 452.1#      | 438.7     | -4.4         |
| <b>RAIL FREIGHT</b> (8/19) billions of ton-miles      | 24.4#       | 24.2      | 2.1          |

**Sources:** American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WPPA, SFPA, Association of American Railroads

## PRICES

|                                                            | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|------------------------------------------------------------|-------------|----------|--------------|
| <b>GOLD</b> (8/30) \$/troy oz.                             | 381.650     | 382.750  | -0.8         |
| <b>STEEL SCRAP</b> (8/29) #1 heavy, \$/ton                 | 146.50      | 146.50   | 8.9          |
| <b>COPPER</b> (8/25) ¢/lb.                                 | 142.5       | 143.4    | 25.8         |
| <b>ALUMINUM</b> (8/25) ¢/lb.                               | 88.0        | 88.8     | 22.2         |
| <b>COTTON</b> (8/25) strict low middling 1-1/16 in., ¢/lb. | 89.77       | 84.99    | 27.8         |
| <b>OIL</b> (8/29) \$/bbl.                                  | 17.92       | 18.54    | 2.1          |

**Sources:** London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                               | LATEST WEEK | WEEK AGO | YEAR AGO |
|-------------------------------|-------------|----------|----------|
| <b>JAPANESE YEN</b> (8/30)    | 98.80       | 96.36    | 99.80    |
| <b>GERMAN MARK</b> (8/30)     | 1.48        | 1.48     | 1.58     |
| <b>BRITISH POUND</b> (8/30)   | 1.54        | 1.54     | 1.55     |
| <b>FRENCH FRANC</b> (8/30)    | 5.07        | 5.07     | 5.39     |
| <b>ITALIAN LIRA</b> (8/30)    | 1626.4      | 1617.5   | 1581.3   |
| <b>CANADIAN DOLLAR</b> (8/30) | 1.34        | 1.36     | 1.37     |
| <b>MEXICAN PESO</b> (8/30)    | 6.298       | 6.270    | 3.384    |

**Sources:** Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

### INSTALLMENT CREDIT

**Friday, Sept. 8, 4 p.m.** ▶ The MMS survey forecasts that consumers probably took on \$9.5 billion more in installment debt in July than they paid off. That would not be much different from the \$9.6 billion added in June, but the increases in both months are much slower than the \$13.1 billion averaged in the three months ended in May. The July slowdown is suggested by the 0.1% drop in retail sales overall and the weakness in car purchases in particular. The recent surge in borrowing has lifted the ratio of installment debt to disposable income to 18.5% in June, near the record peak of the late 1980s. Revolving debt, which includes credit cards, is leading the runup.



# This Week, Online

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## Sunday

Investing in emerging markets, where rewards and risks can both be high: Talk with BW's William Glasgall. **Sept. 3 9 p.m. EDT in the Globe**

## Monday

A very special Labor Day with Labor Secretary Robert Reich, in a dialogue with the American worker. **Sept. 4 8 p.m. EDT in AOL Live**

## Wednesday

Is the U.S. economy heading for recession? Talk with forecaster David Levy and BW's William Wolman. **Sept. 6 8 p.m. EDT in the Globe**

## Thursday

Designing for the interactive world: Chipp Walters of award-winning Human Code joins BW's design maven Bruce Nussbaum. **Sept. 7 9 p.m. EDT in the Coliseum**

*Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event*

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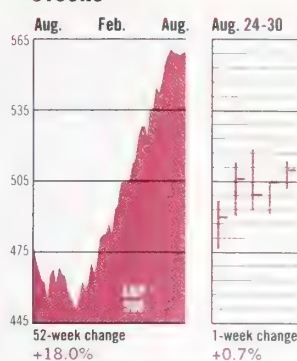


# Investment Figures of the Week

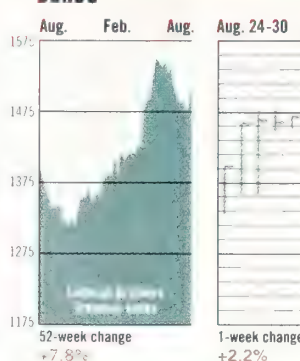
## MENTARY

a week! First, Microsoft Corp. shares Windows 95. Then, the billion Chase Manhattan Corp. chemical Banking Corp. merger the banking world. And then Warner Inc. jumps into the rs and acquisitions fray with billion offer for Turner Broad- ing System Inc. The stock marded the week up 24 points, at 6. Bond traders were kept on es as slowing durable goods and sagging retail sales ened inflation fears, sending old on the 30-year Treasury from 6.91% to 6.69%.

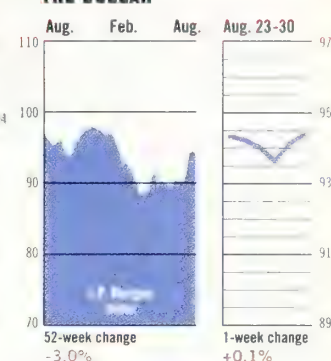
## STOCKS



## BONDS



## THE DOLLAR



## MARKET ANALYSIS

### STOCKS

|                                        | Latest | % change<br>Week | % change<br>52-week |
|----------------------------------------|--------|------------------|---------------------|
| DOW JONES INDUSTRIALS                  | 4604.6 | 0.4              | 17.7                |
| DOW JONES COMPANIES (S&P MidCap Index) | 209.7  | -0.4             | 17.5                |
| DOW JONES COMPANIES (Russell 2000)     | 303.3  | -0.4             | 17.9                |
| DOW JONES COMPANIES (Russell 3000)     | 323.3  | 0.5              | 18.3                |

### ASIAN STOCKS

|                                      | Latest   | % change (local currency)<br>Week | % change<br>52-week |
|--------------------------------------|----------|-----------------------------------|---------------------|
| DOW JONES ASIA (FINANCIAL TIMES 100) | 3504.0   | -0.3                              | 7.8                 |
| DOW JONES NIKKEI INDEX               | 17,983.9 | 1.4                               | -12.8               |
| DOW JONES TSE COMPOSITE              | 4531.2   | -1.7                              | 4.2                 |

### FUNDAMENTALS

|                              | Latest | Week ago | Year ago |
|------------------------------|--------|----------|----------|
| 90-DAY TREASURY BILL YIELD   | 5.44%  | 5.59%    | 4.66%    |
| 30-YEAR TREASURY BOND YIELD  | 6.69%  | 6.91%    | 7.45%    |
| S&P 500 DIVIDEND YIELD       | 2.40%  | 2.42%    | 2.67%    |
| S&P 500 PRICE/EARNINGS RATIO | 16.2   | 16.0     | 18.9     |

### TECHNICAL INDICATORS

|                                           | Latest | Week ago | Reading  |
|-------------------------------------------|--------|----------|----------|
| S&P 500 200-day moving average            | 506.7  | 504.3    | Positive |
| Stocks above 200-day moving average       | 74.0%  | 74.0%    | Negative |
| Speculative sentiment: Put/call ratio     | 0.61   | 0.56     | Neutral  |
| Insider sentiment: Vickers sell/buy ratio | 2.39   | 2.31     | Neutral  |

BLOOMBERG FINANCIAL MARKETS

## INDUSTRY GROUPS

### MONTH LEADERS

|                            | % change<br>1-month | % change<br>12-month |
|----------------------------|---------------------|----------------------|
| BROADCASTING               | 9.1                 | 23.2                 |
| PROPERTY-CASUALTY INSURERS | 8.8                 | 26.0                 |
| MULTI-LINE INSURERS        | 6.8                 | 28.7                 |
| MONEY CENTER BANKS         | 6.4                 | 30.2                 |
| PACKAGING                  | 6.3                 | -10.7                |

### Strongest stock in group

|                          | % change<br>1-month | % change<br>12-month | Price   |
|--------------------------|---------------------|----------------------|---------|
| CAPITAL CITIES/ABC       | 20.0                | 38.6                 | 115 1/8 |
| GENERAL RE               | 12.0                | 33.3                 | 149 5/8 |
| CIGNA                    | 14.8                | 39.2                 | 94 1/8  |
| CHEMICAL BANKING         | 14.2                | 50.3                 | 59 3/8  |
| CONSOLIDATED FREIGHTWAYS | 11.0                | 12.8                 | 26 1/2  |

### MONTH LAGGARDS

|                             | % change<br>1-month | % change<br>12-month |
|-----------------------------|---------------------|----------------------|
| SPECIALTY APPAREL RETAILERS | -8.7                | -19.1                |
| POLLUTION CONTROL           | -7.5                | 0.1                  |
| DRUG CHAINS                 | -6.9                | 26.5                 |
| SEMICONDUCTORS              | -6.9                | 68.2                 |
| SPECIALTY RETAILERS         | -6.8                | -7.1                 |

### Weakest stock in group

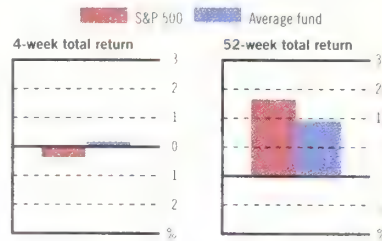
|                            | % change<br>1-month | % change<br>12-month | Price  |
|----------------------------|---------------------|----------------------|--------|
| GAP                        | -9.9                | -27.1                | 32     |
| BROWNING-FERRIS INDUSTRIES | -12.0               | 4.2                  | 33 1/8 |
| WALGREEN                   | -9.4                | 26.7                 | 24     |
| INTEL                      | -12.3               | 78.1                 | 58 1/8 |
| WOOLWORTH                  | -17.5               | -18.1                | 13     |

## MUTUAL FUNDS

MORNINGSTAR INC.

### LEADERS

|                                    | %    |                                     | %     |
|------------------------------------|------|-------------------------------------|-------|
| 4-week total return                |      | 4-week total return                 |       |
| INTECK ASIA INFRASTRUCTURE A       | 11.0 | WRIGHT EQUIFUND-GERMANY             | -6.2  |
| INDIAN UTILITY                     | 7.6  | WRIGHT EQUIFUND-BELGIUM/LUXEMBOURG  | -5.7  |
| BARBURG PINCUS ADVISOR JAPAN OTC   | 7.3  | WRIGHT EQUIFUND-NETHERLANDS         | -5.2  |
| 52-week total return               |      | 52-week total return                |       |
| ELIGMAN COMMUNICATIONS & INFORM. A | 95.0 | WRIGHT EQUIFUND-MEXICO              | -50.0 |
| JOVETT SMALLER COMPANIES A         | 89.5 | BT INVESTMENT LATIN AMERICAN EQUITY | -36.2 |
| DELITY SELECT ELECTRONICS          | 85.9 | TCW/DW LATIN AMERICAN GROWTH        | -35.6 |



## RELATIVE PORTFOLIOS

DRUM/ALGRAW-HILL

Percentages represent the percent value of \$10,000 invested one year ago for each portfolio.

Percentages indicate daily total returns.



U.S. stocks

\$12,098

+0.09%



Treasury bonds

\$11,828

+2.30%



Foreign stocks

\$10,890

-0.28%



Money market fund

\$10,533

+0.12%



Gold

\$10,010

+0.26%

Data on this page are as of market close Wednesday, Aug. 30, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close Aug. 29.

Mutual fund returns are as of Aug. 25. Relative portfolios are valued as of Aug. 29. A more detailed explanation of this page is available on request. r=revised NA=Not available



## BIGGER, SURE. BETTER? WELL...

**I**s bigger good or bad? That's the question on the minds of a host of people in America these days, from media moguls and banking CEOs to politicians, foreign competitors, and average citizens wondering about jobs, delivery of services, and prices (page 34). Like it or not, corporate bigness is destined to become one of the hottest public-policy questions in the years ahead. A new wave of mergers and acquisitions is generating the kind of mass and concentration unseen on the economic front since the late 19th century.

The great irony is that much of this race to bigness is being propelled by the same information technology that futurist Alvin Toffler and other techno-libertarians predicted would lead to smallness—empowering individuals and entrepreneurs to work independently on the Internet with speed and flexibility unmatched by Big Business. Big is supposed to be dead.

Forget it. Corporate America is discovering what the military has known for at least a decade: that information technology allows for much more effective command and control of size and complexity. And most big companies that want to get bigger have the green light: Washington will permit it, and Wall Street will finance it.

So industry after industry is finding bigness a solution to its problems. Banks look to mergers for cost-saving. Media com-

panies try to lock in distribution and product. Retailers striving for economies of scale. Transportation, utilities, telecom, consumer goods, pharmaceuticals, and software are moving to consolidate, concentrate, and grow bigger.

But the fact that bigness is seen as the salvation for every business problem makes the current merger wave suspect. The monopoly wave of the turn of the century, the oligopoly wave of the 1920s, the conglomerate wave of the 1960s, and the debt-fueled wave of the 1980s all ended in a burst of excess and the dashed dreams of many an empire builder.

The markets, good trustbusters by and large, will determine whether bigness has once more gone too far. It may be that in the new global marketplace, the need for size has grown significantly. For new bigger companies, much will depend on whether managers can work the information flow within behemoth corporations. But markets must remain free to act. They will give the only reliable signals of whether new information technology and globalization mean that U.S. companies must get ever bigger to succeed.

This is the question that politicians also ponder. Already a chorus of complaint against Big Business can be heard on the sidelines from both conservatives and liberals who blame it for exporting jobs and keeping wages stagnant. Bigness is a hot issue, once again.

## EMERGING MARKETS CAN BE A SNAKE PIT

**B**ack in 1993, they were called “emerging” markets. Following the Mexican meltdown in late 1994, they became “submerging” markets. Now, the stock and bond markets of Latin America and Asia are once again being heralded—this time as “reemerging” markets. Let's hope they get it right this time.

For the sake of widows and orphans and the rest of us who find pension fund managers investing our retirement money in what used to be called the Third World, a little sanity and savvy is in order. Blindly throwing cash at emerging markets in an effort to chase higher rates of return was a costly mistake. Fiduciary responsibility, if not simple common sense, requires a more level-headed approach.

Take the notion of risk. During the last round of overseas investment, there wasn't much awareness of it. Carried away by the globalization of the market economy and high growth rates, money managers socked nearly \$100 billion into Mexico, China, Taiwan, Argentina, Chile, etc., over three years. With deregulation, privatization, and foreign investment, the economic opportunities in these countries appeared endless.

Then reality struck. Politics, ignored by the money managers, overwhelmed economic considerations in Mexico, as an election led to financial manipulation. Mexican capital began to flee, followed by U.S. and other foreign “hot” money. The

peso collapsed, cratering stock markets around the emerging market world. These markets are now on the rebound, but they have yet to fully recover (page 68).

It certainly makes sense to invest in the 3 billion new customers entering the global economy. Growth rates will be higher than in the more mature economies of the West for decades to come. Some of the best prospects for healthy earnings are in emerging markets.

But the risk/reward ratio remains higher in Latin America and Asia, and money managers should recognize this as a hard fact. Taiwan's economy is booming, but its stock market is off 40% this year. China is so angry at Taipei's moves toward greater independence that it is testing missiles just 100 miles offshore. The military is challenging the civilian government in Chile. Argentina's Finance Minister is talking darkly of corrupt “mafias,” and a religious party recently canceled a key energy deal with a U.S. company in India.

Money managers taking a second shot at higher returns in emerging markets would be wise to hire a few political risk analysts, a couple of area specialists, and even one or two people who know something about military affairs. Political stability is as important as economic opportunity when investing in societies striving to make the difficult transition to capitalism and democracy. Growth is not enough.



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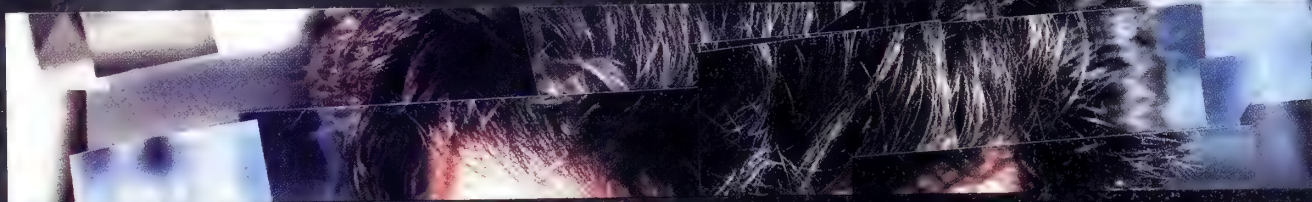
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# BusinessWeek

SEPTEMBER 18, 1995

A PUBLICATION OF THE MCGRAW-HILL COMPANIES

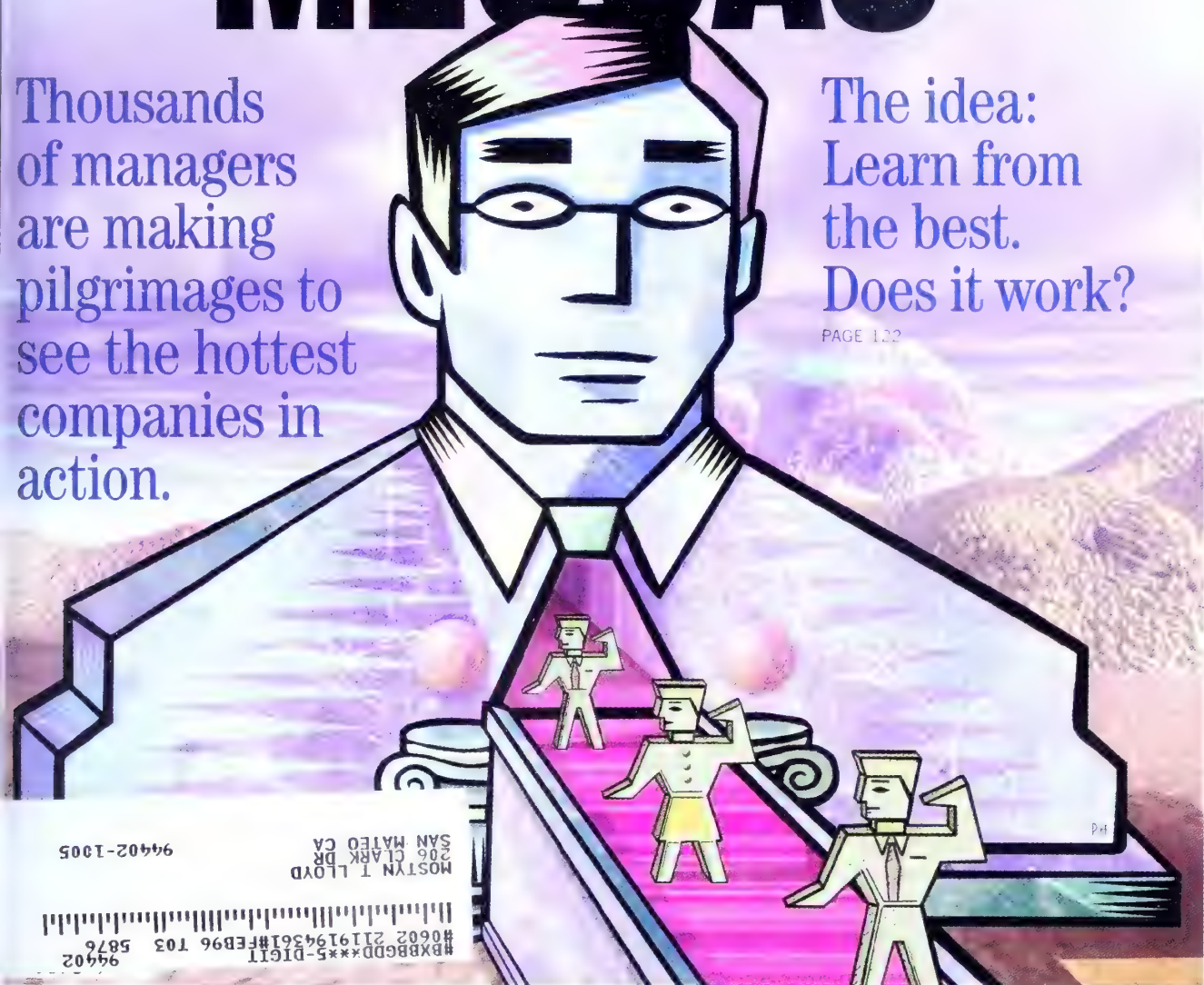
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## MANAGEMENT MECCAS

Thousands  
of managers  
are making  
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see the hottest  
companies in  
action.

The idea:  
Learn from  
the best.  
Does it work?

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# BusinessWeek

SEPTEMBER 18, 1995

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Once upon a time, executives flocked to Japan for lessons. Now, American cult companies are the big draw for would-be reengineers

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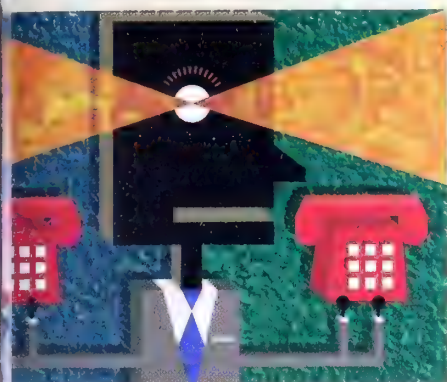
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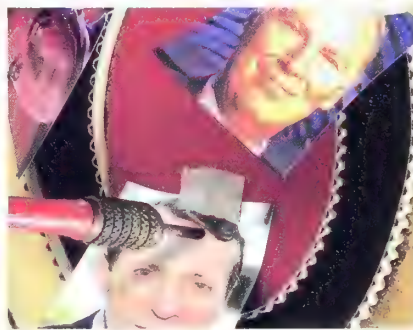
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# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

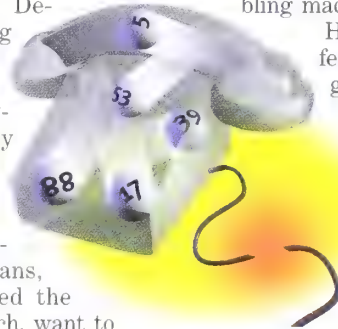
## CASINO SOCIETY

### ODDS ARE AGAINST THIS LOTTERY

THE PLANNED NATIONAL Indian Lottery is having trouble going national. Minnesota Attorney General Hubert Humphrey III has told AT&T, MCI, and Sprint they may not offer this phone-in lottery in his state. All three say they will comply. Several other states intend to follow his example. In Congress, Representative Robert Torricelli (D-N.J.) is out to thwart the enterprise, questioning the legality of

transmitting gambling information interstate.

The weekly lottery aims to start in December, using a 24-hour 800 number, where players may charge bets of at least \$5. Idaho's Coeur d'Alene Indians, who unveiled the plan in March, want to operate in Washington, D.C., and the 36 states that have their own lotteries. Estimated weekly jackpot: \$20 million.



**TALK SHOW** "If he were to decide to run in November, that would clearly make it less likely I would run."

—House Speaker Newt Gingrich, on a Colin Powell Presidential bid

## PUBLISHERS ROW

### UNEARTHLY RATES FOR GHOSTWRITER

GHOSTWRITING A BEST-selling business book is getting more expensive. At the Queen of Ghostwrite Donna Sammons Carpenter She and the two dozen writers at her Boston-based firm Wordworks, helped pen the megasellers *Reengineered the Corporation* by Michael Hammer and James Champy, *The Pursuit of Wow* by Tom Peters, and *The Discipline* by Michael Treacy and Fred Wiersema. Wordworks, says Treacy gives editorial assistance that publishers no longer grant. Wordworks can discreetly write, edit, or

## WHEELER-DEALERS

### 'LORENZO AT 12 O'CLOCK HIGH'

FRANK LORENZO'S LATEST airline foray is running into back-ack from the feds. The Transportation Dept. wants to meet with tiny Nations Air Express of Smyrna, Ga., and Lorenzo to talk over his involvement with the air carrier. The department says that Nations Air documents detail a series of possible transactions between the airline and Lorenzo's companies.

control over Nations Air, which started operations in March. The department last year rejected his bid to re-enter the airline business with the startup carrier he controlled, ATX. It found ATX unfit to fly because of concerns about safety and management problems at Conti-

nental and Eastern under Lorenzo's leadership. Lorenzo blamed the feds' opposition on pressure from a pro-labor Clinton Administration and unfair attacks from unions. Nations Air declines to comment on what it calls a "private matter." The airline, which flies two 737-200 jetliners, offers low-fare service to Pittsburgh, Philadelphia, Boston, and Myrtle Beach, S.C.

Wendy Zellner



**'LAK BAIT:** The wrong stuff?

"There's already been some loans and

some management expertise provided" dating back to early this summer, says a Transportation official, who declined to reveal the size of the loans. The documents indicate Lorenzo's companies contemplate gaining an ownership stake, the official says.

Transportation worries that Lorenzo, who could not be reached for comment, may already be exercising some

## THE LIST HIGH-TECH FEVER

In a year of flashy initial stock offerings, high-tech companies are the showiest.

Renter's Choice, which leases

furniture, is the lone nontech entry among the Top Ten IPOs. No.1 Premisys makes telecom gear. Unlisted: Internet

software maker Netscape, whose IPO had a huge first-day run-up Aug. 9, but is now up a mere 75%. The latest buzz:

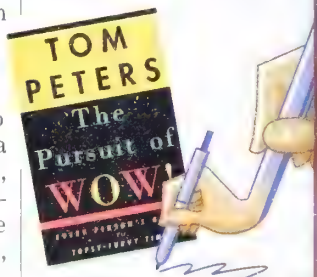
Kohlberg Kravis Roberts' Sept. 5 news it's selling shares in its (nontech) publisher, K-III.

### LEADING IPOs OF 1995

|                              | OFFERING DATE | PRICE CHANGE* |                 | OFFERING DATE | PRICE CHANGE* |
|------------------------------|---------------|---------------|-----------------|---------------|---------------|
| PREMISYS                     | 4/5           | 426%          | OAK TECHNOLOGY  | 2/13          | 214%          |
| RENTERS CHOICE               | 1/25          | 357           | ARCSYS          | 6/6           | 211           |
| INTEGRATED SILICON SOLUTIONS | 2/2           | 276           | AG ASSOCIATES   | 5/15          | 179           |
| SEMITOOL                     | 2/2           | 249           | ASM LITHOGRAPHY | 3/15          | 169           |
| UUNET                        | 5/25          | 222           | STORMEDIA       | 5/4           | 159           |

\*From offering date through Sept. 1, 1995

DATA: SECURITIES DATA CORP.



even research a book. Peters provides a manuscript for Wordworks CEO Carpenter edits. Others make tape recordings that Wordworks converts into book form.

Today's rates: typically \$60,000 for a book proposal or \$300,000 to produce a book from scratch. The 1993 *Forbes* magazine helped on *The Portable MBA Desk Reference*, edited by Paul Argenti: about \$50,000. Also, Wordworks gets royalties up to 20%. "You'd have to be crazy to pay that kind of money," says Roger Straus, CEO of Farrar Straus Giroux. Upcoming Carpenter authors: Mike Milken and Senator John Kerry (D-Mass.). "We're expensive, but we're worth it," says Helen Reilly, Wordworks president, who won't comment further on fees.

Willy Ste





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# Up Front



**MAKING HAVANAS:**  
*A proletarian puff*

the first increase in two decades. While many restaurants have banned smoking, cigar bars are suddenly chic. U.S. demand for quality Cuban Habana Puros, Cohibas, and Montecristos is such that *Cigar Aficionado* magazine estimates up to 10 million cigars leave the island yearly for this country in defiance of the U.S. ban on Cuban imports. Americans may buy up to 100 Cuban cigars at a time in countries other than Cuba, but any amount over that runs the risk of confiscation by U.S. officials.

In the Key West case, two men were charged with smuggling, conspiracy, and violating the Trading With the Enemy Act. One pleaded not guilty, the other has yet to be arraigned. As for the cigars, Customs officials say they will be burned—but not smoked. *David Swafford*

## NEW WORLD ORDER

### "PSST! I GOT THAT GOOD CUBAN LEAF"

THE DUFFEL BAGS CARRIED off the 37-foot fishing boat and onto a Key West dock looked suspicious to U.S. Customs Service agents. When they swooped in, the officers didn't find drugs. Customs says the swag was 2,700 hand-rolled cigars that the suspects bought for \$3,600 in Fidel Castro's Cuba and could sell for \$28,000 in America.

Smuggling Fidel's finest is on the rise because premium-cigar smoking is undergoing a renaissance. In 1994, non-Cuba imports expanded 5%,

## BUSINESS SPEAK

### THE TIGER TEAM IS MIND-MAPPING

CORPO-BABBLE IS GETTING more arcane all the time. Or so says consultant Walter Polsky, head of Chicago-based Cambridge Human Resource Group, who is compiling a dictionary to help the uninitiated interface with colleagues without losing face.

## DEFINE...

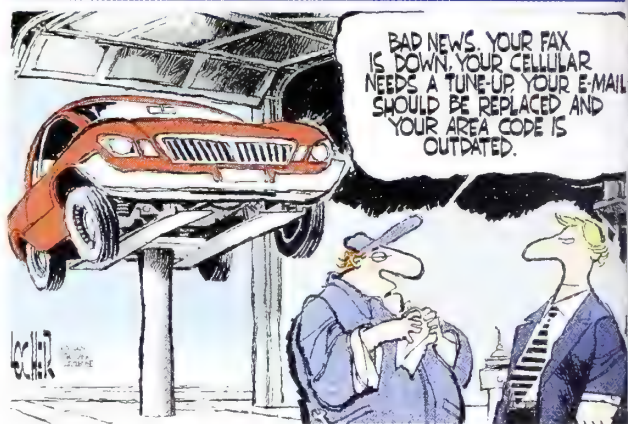
- ▶ **DOWNSCOPING**
- ▶ **JOB MORPHING**
- ▶ **MIND-MAPPING**
- ▶ **TIGER TEAM**
- ▶ **YOU INC.**

DATA: CAMBRIDGE HUMAN RESOURCE GROUP

Let's try "downscoping." That's when a company sheds subsidiaries unrelated to its core business. Then there's the military-like "tiger team," specialists who cut through layers of bureaucracy to solve problems. They may try "mind-mapping," or solo brainstorming. These days of-

ten call for "job morphing"—changing your job and skills to meet new work requirements. The workplace ideal is a "You Inc." type: flexible, eager for extra work, and self-promotional. Also, usually unlikely to be laid off. □

## DRAWN & QUARTERED



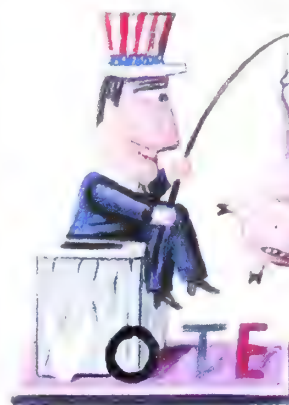
## TAXES AT WORK

### PEGGING THE POWER OF PORK

PORK PAYS OFF IN VOTES. POLS have long known this, but now, two economists have done a study to prove that empirically and to estimate how much pork it takes to

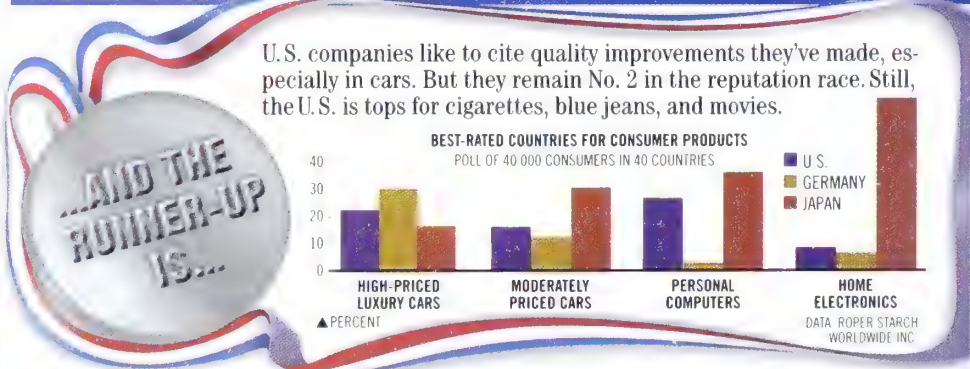
bent. Pork encompasses such things as highways, defense contracts, and job programs—not entitlements in the order of welfare, which are delivered by a formula. "There's no doubt pork is rewarded," says Harvard University's Steven Levitt, with fellow economist James Snyder Jr., compared congressional tallies with federal projects from 1983 to 1990.

Interestingly, the study found the political power of pork prevails whether the district is Republican or Democratic. May that's why lawmakers on both sides of the aisle are reluctant to give up spoils, despite cries on Capitol Hill about cutting fat from the federal budget. If pork were eliminated, says Levitt, House incumbents whose 1994 election victories were close could very well lose next time. And that's a lot of people: 10% of incumbents with less than 55% of the vote. *Mary Beth Regan*



win one vote. They found that each \$100 spent per person in a congressional district for discretionary federal projects translates into 2% of the popular vote for an incumbent.

## THE BIG PICTURE



**FOOTNOTES** U.S. trade deficit with China during 1994's first half: **\$11.7 billion**. 1995's: **\$14.4 billion**

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## HANDICAPPING DISNEY'S MIKE AND MIKE SHOW

Your article "Disney: Room for two Lion Kings?" (News: Analysis & Commentary, Aug. 28) is very puzzling. Michael Eisner hires Michael Ovitz as president, but of what? The story points out that Eisner's top two executives, Sanford Litvak and Stephen Bollenbach, will continue to report to Eisner. Another executive, Joe Roth, has been assured "that this [live-action film business] company is my company to run." How many other executives received similar assurances? Working for a control freak with a tough management style who clashes with subordinates—I give Ovitz a year!

Richard J. Cronin  
Rosemont, Ill.

## WHEN OFFICEHOLDERS ARE STOCKHOLDERS, WATCH OUT

Your article on congressmen who own stock in companies influenced by congressional decisions ("How are you voting? What are your stocks?", Finance, Aug. 28) was timely and hard-hitting. The continued success of free markets and vigorous capital formation in our nation depends on honesty and fairness by those we elect. When scalawags are content to profit from such conflict-of-interest situations, as you report, it is high time for the voters to toss them out of office.

Jake Schwartz  
Petaluma, Calif.

Although your article on congressional trading was insightful and pointed out real examples where conflict of interest was obvious, using Senator Don Nickles (R-Okla.) as one of the "star" perpetrators weakened the story. It seems far-fetched to me that Senator Nickles would introduce a bill and go through all the hassles, possible backlash, and so on for a \$6,500 investment. It's more likely that he introduced the bill because Oklahoma—with its large oil-and-gas industry struggling to com-

## CORRECTIONS & CLARIFICATIONS

In "Unproven, but dazzling" (Information Processing, Sept. 4), the capacity of Qualcomm Inc.'s new cellular-phone factory will be 1 million units a year by yearend.

In "Balance sheets that get well soon" (The Corporation, Sept. 4), Dr. Melvin A. Mackler's correct title is vice-chairman of the board at South Miami Hospital, and the correct spelling of the city manager's name in Tallahassee, Fla., is Costa S. Vatikiotis.

In "The Newtniks have seen the future. So do they think" (Information Processing, Sept. 11), Arno A. Penzias should have been identified as vice-president for research at AT&T Bell Laboratories.

"The lethal side effects of managed care" (Economic Viewpoint, Aug. 7) should have said that Foster Higgins & Co., an employee-benefits consulting firm, was the source of the finding that employers' health-care costs fell 1.1% in 1994.

pete with rivals abroad—would benefit. The other examples you cited, which involved tens or hundreds of thousands of dollars, seemed much more plausible.

Marjorie A. Hottel  
Orem, Utah

If 14-year-old Sam Bond [who owns up to \$15,000 in McDonnell Douglas stock] did not have insider information from his father, Senator Christopher Bond (R-Mo.) [who sits on the Senate subcommittee that sets defense spending], I will eat my broker's hat.

Emily Gordon  
Abu Dhabi  
United Arab Emirates

## WINDOWS 95: ONE RETAILER IS SKEPTICAL

As the operator of a 23-year-old computer store, I was kind of dreading the release of Windows 95. The constant barrage of hype on CNN and other ne-

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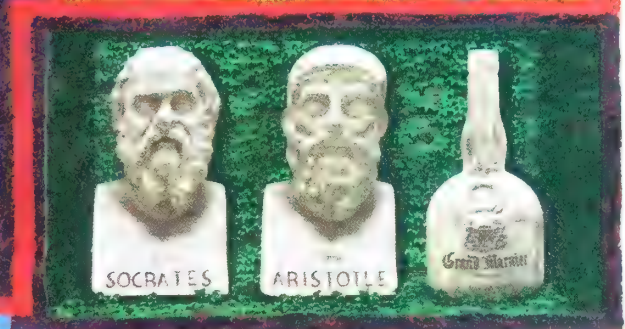
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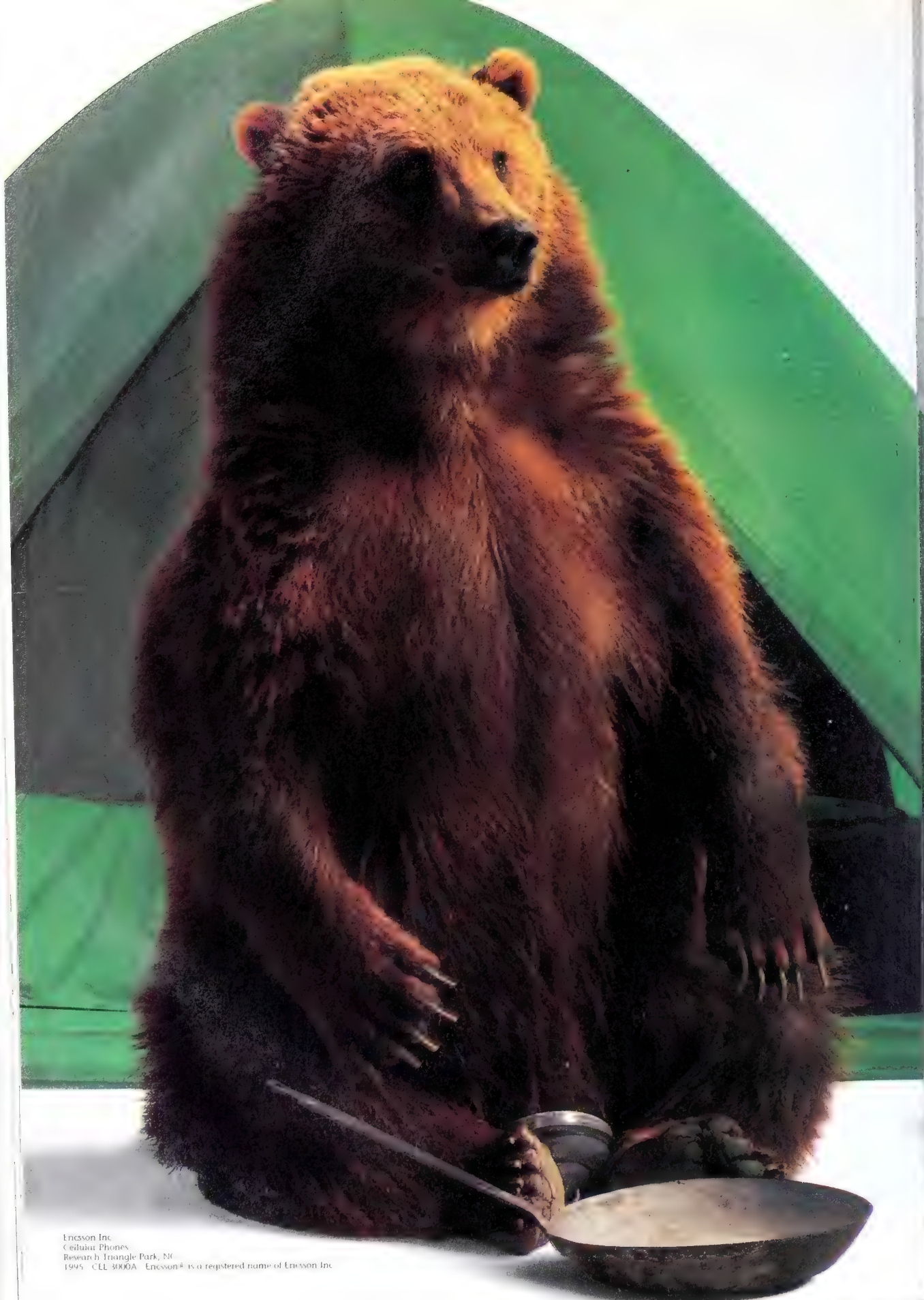






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works gave one the expectation of the Second Coming ("Feel the buzz," News: Analysis & Commentary, Aug. 28). Therefore, I was surprised that our store did not receive one single phone call concerning Windows 95 on the Thursday of its launch and that we did not have very many requests for the software.

The feeling of most of our customers, and ourselves, is that we will take a wait-and-see attitude. One of the reasons most dealers are indifferent is that our wholesalers will sell us copies of Windows 95 for \$90, which, with freight and COD charges, can add up to \$110. With Microsoft telling everyone that the street price is \$89, and Wal-Mart selling Windows 95 for less than \$89, it's no wonder that most computer stores are not interested in taking on hassles and losing money at the same time.

Steve Dendrinis Jr.  
President  
Computer King  
Knoxville, Tenn.

## 'TIS BETTER TO GIVE IF YE RECEIVE

Great. Corporate America downsized with a frenzy and left already cash-strapped charities with the task of caring for the millions who were made jobless by its "bottom-line" tactics. And now, it is telling those charities that they will have to "give something back" if they want donations ("Giving—and getting something back," Social Issues, Aug. 28).

Go after the churches next, guys. Don't give those cathedrals and chapels a nickel unless they see to it that their parishioners wear, use, drink, or eat your brands.

H. Lee Martin  
Piedmont, Calif.

## MAGGIE DIDN'T CURE THE "BRITISH DISEASE"

Sadly, your review of Charles Dellheim's *The Disenchanted Isle: Mrs. Thatcher's Capitalist Revolution* (Books, Aug. 28) peddles many of the distortions of Britain's New Right. When Mrs. Thatcher came to power, inflation was not at 22%, nor was unemployment at 15%; both were much lower. They reached such dizzying heights only after a year or two of Mrs. Thatcher's economic experiments.

And not even Mrs. Thatcher would pretend that the "British disease" was exclusively due to socialists' spending too much on the National Health Service, defense, housing, and social security. The private sector, particularly man-

ufacturing, had long been weak and inefficient. For generations, supposedly intelligent Brits have avoided wealth-creating activities.

Without doubt, Mrs. Thatcher made some improvements around the edges. But it is doubtful if Britain's cultural malaise has really been cured, let alone seriously analyzed.

Henry Tinsley  
Tinsley Foods Ltd.  
Peterborough, England

## SPIEGEL MAY HAVE A WEENSY CUSTOMER-RELATIONS PROBLEM

While "Can Spiegel pull out of the spiral?" (Marketing, Aug. 28) presented many valid reasons why Spiegel might be having problems, this totally frustrated shopper can offer one other: Buy-

### SPIEGEL STUMBLES

"After five months of phone calls, correspondence, and threats of legal action, I got the mess resolved. I finally cut up my charge card and sent it back"

ing from the Spiegel and Eddie Bauer catalogs is amazingly difficult. Either the product is not in stock, only partially in stock (for example, only the blouse of a two-piece dress), or will seem to be in stock when ordered but then turns out to be out of stock by the time (if one is lucky) that part of the order is sent. I got an outfit from Spiegel this summer—two months after I ordered it. Add to this that I get no response to complaint letters, and one has little incentive to buy from either catalog. I toss them in the trash now, since the aggravation just isn't worth it.

Fortunately, there are other catalog merchandisers with better customer service, so I patronize them.

Christina M. Kampman  
Donnelsville, Ohio

Spiegel's problems don't surprise me. I was a long-standing customer until this year. I placed an order through the catalog in November, 1994, and never received the goods. After five months of phone calls, correspondence, and threats of legal action, I got the mess resolved. I finally cut up my charge card and sent it back. Retailers need to realize that price is not always the reason customers go elsewhere.

Bonnie Barnett  
Bakersfield, Calif.

Your article on Eddie Bauer's problems might have used this sad-but-true story: I tried to place a phone order with my Discover credit card (because it gives a discount). They don't accept it. Stated reason: Hadn't gotten computers changed yet!

Walker H. Thorpe  
Boulder City, Nev.

## WORK LONGER, SAVE MORE, AND RETIRE WITH CONFIDENCE

Rudi Dornbusch discovered that populations age, the economic cost supporting retirees rises ("And you thought Social Security was in trouble..." Economic Viewpoint, Aug. 28). But he implies that the higher cost somehow be avoided if we'd all just put more money into defined-contribution pension plans.

By itself, however, that would not reduce the fraction of our national income that must go to support the aged in future years. Nor would it insulate world capital markets from the impact that Dornbusch fears. Any reduction in future government borrowing would be more than offset by the cashing out of assets accumulated by the future retirees.

Aging societies can avoid sizable increases in the burden of supporting their retirees only by requiring longer careers or reducing the relative living standards of those who reach retirement age. A great amount of shuffling of financial assets can hide that simple truth.

Lawrence H. Thompson  
Alexandria, Va.

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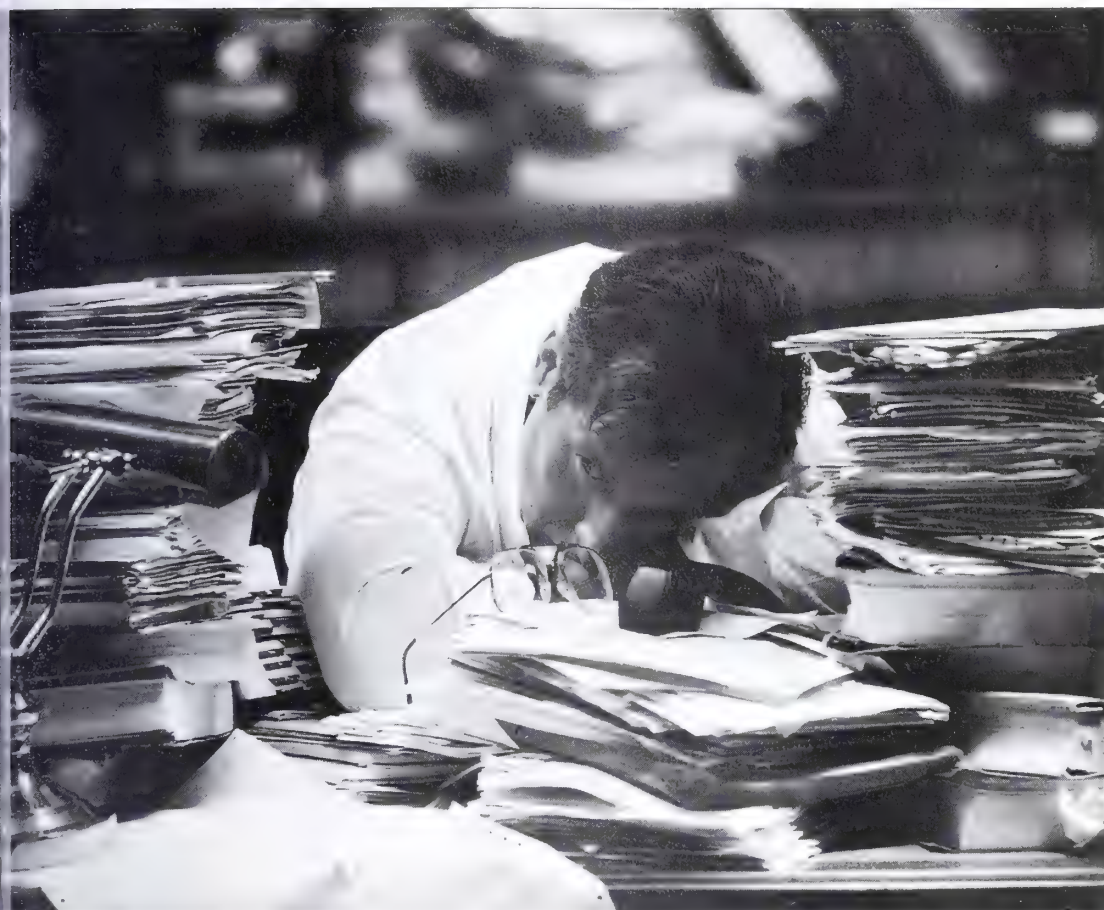
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**GOING UPTOWN:** Work on a tugboat involves long shifts—but good food

## ON A TUG: CENTER STAGE IN A BRINY BALLET

**‘C**over your ears,” yells the tugboat’s chief engineer as he grins a crooked grin. “What?” I scream back, just in time to be jolted by a boom that sounds to me like a Space Shuttle launch. It’s only the engine starting up, he mouths, as I jam my hands over my ears. Eddie Christensen is used to it. After more than 35 years as a tugboat engineer, it’s a sound as familiar to him as the currents lapping against the bow.

I scan this noisy, hot pit of machinery that looks more like a contraption from a Dr. Seuss book—not what I had ever imagined the engine room of a tugboat would look like. A generator hums while the 3,300-horsepower engine warms up. A switchboard lights up to show any electrical mishaps. On the sides of the walls, metal tubing circulates salt water that cools the machinery.

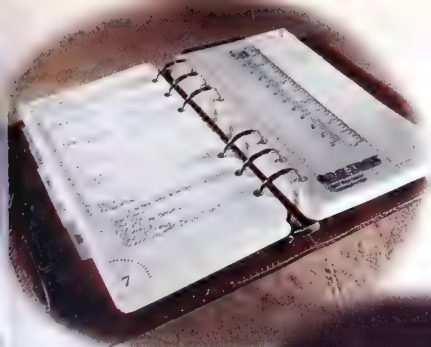
This is Eddie’s home away from home. Eddie and the four other members of the Margaret Moran crew spend two weeks on the tug, working 12 hours on and 12 hours off. Then, they have a week off before another two-week hitch.



Eddie is 66, but the work along the terways of the New York Harbor kept him fit. His legs, for example, had to be as sturdy as any 30-year-old’s from constantly running up from the engine room to the deck to keep on top of things. He has been engineer on the Margaret Moran since 1986 and worked for Moran Towing & Transportation Co., a top operator of tugs on the East Coast, since 1957.

**“STRANGE FACE.”** Much has changed since that time. Although the harbor still berths ocean liners and cargo ships from around the world, it’s a shadow of its former self. Rival West Coast ports like Los Angeles and Long Beach are grabbing Pacific Rim trade, Baltimore and Norfolk are fighting for business, and the great liners are mostly gone. The U.S. Navy left the Brooklyn Navy Yard, and other shipyards are silent.

But on this hazy summer morning, the harbor sure looks busy. The waterways are speckled with barges, U.S. Coast Guard cutters, freighters, ferry tour boats, and cabin cruisers. Yet old salts such as Eddie remember when the now-rotting piers along the Hudson were so crammed that it was like trying



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# Letter From New York

to find a parking space in midtown.

Sitting comfortably at the helm, smoking a cigarette, is Gene Poissant, captain of the Margaret Moran. As the Manhattan skyline fades in the haze, the tug makes its way out of the upper harbor and past the Statue of Liberty. "We get jaded about it, but God, it is beautiful," he says, steering the tug with cavalier ease, his tanned hands loosely curled over two levers that control the engines. "Some mornings, when we're coming through the fog, she just comes out of nowhere."

Poissant is a gruff man with a dry, snappy sense of humor. He has a nickname and a story for every tug captain he passes. He calls one old captain the Cadaver. A boat with the name Jacqueline A passes. "A strange face," Poissant says, explaining that new vessels stick out because the harbor is like a neighborhood—the captains know everyone on the block.

Our first job of the morning is docking a container ship at Port Elizabeth in New Jersey. The Port Authority of New York & New Jersey operates the port for both states, but Manhattan and Brooklyn long ago lost the big freight business to the more modern facilities on

the Jersey side, and the city has been trying ever since to get some of the business back—to little avail. In late August, a City Planning Dept. study raised the question of whether New York should continue pouring money into its money-losing terminals.

**CREAMED CORN.** Within 15 minutes, we are suddenly dwarfed by the 700-foot-long Saudi Makkah out of Dammam, Saudi Arabia. You can still make out its former identity—as a ship of Polish registry—from old, painted-over raised letters. The two vessels are introduced gingerly. The Margaret Moran is encased in thick black rubber—sidings and old tires. (A rusty gash on the Saudi Makkah's side is the handiwork of the unprotected bow of some ill-steered tug, Poissant notes.) Because the container ship is so huge, it needs another tug to help maneuver it toward the pier.

This is a routine job for Gene, but he still waits for orders from the Moran-contracted pilot, Kevin Gadow, who has climbed way up a ladder to the Saudi

ship. After an hour of nudging and wheeling and sloshing water and a doled orders, the docking is done, signaled by the pilot. To me, it seemed like a very smooth job. I ask Poissant he is always so relaxed. "It's just like driving on the road," he says.

It's a telling comparison. The harbor has rules just like a highway—and



share of jerks. However, these day traffic jams are rare. Twenty-five years ago, 10,338 passenger and freight ships were logged into the harbor. In 1990, there were 6,085, and Moran handled 50% of them. Last year, the number had dropped to 4,537, and Moran's share to 39%.

On the bridge, I'm removed from the groaning steel and sweltering busywork. The air conditioner in the pilot house breathes cool air, and down below to

## Prose.

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Khanda is preparing our lunch, which turns out to be a real feast: steak with baked potatoes, creamed corn, homemade chocolate chip cookies. I'm impressed, but I'm told this is nothing in comparison to when a full-time chef had to cook elaborate meals for them. "All you could eat," Poissant says. Things changed in 1988 when, because of declining business, Moran cut perks, amenities and overtime pay and changed the work schedule from one

hours. "Just about the time that we start getting after each other, I have to go back to work," Poissant jokes.

While business may be off for the tugs and for the City of New York, the Port Authority of New York & New Jersey says that more cargo is actually coming in. It's just coming on fewer, but larger container ships. New \$19.5 million rail facilities in Port Elizabeth will nearly double the amount of containers that can be loaded and unloaded directly onto rail shipments to and from eastern Canada and the Midwest. Already, that helped the port snag the Hyundai Corp. car account away from Portland, Ore.

If the New York port hopes to fend off West Coast rivals, particularly Long Beach-Los Angeles, which have naturally deeper waters, it will need much more dredging to accommodate the current crop of super-ships the Asian yards specialize in building. Easier said than done in this era of ecological concern: After years of struggle by environmentalists, the harbor's striped bass fishery is just now making a comeback.

Poissant isn't optimistic about the fu-

ture of the harbor but stays because he's stubborn, he says. And he clearly loves the water. "I did trucking for a year, but it just wasn't the same," Poissant recalls. Little wonder: New York City brine was the first thing he ever smelled. "I was born on a coal barge in 1938. My mother couldn't get off of the barge because of a storm, so the doctor came on board and delivered me."

**UNHEEDED ADVICE.** Poissant is actually a third-generation tugboat man. His father quit sixth grade in order to toil on the tugs, but later warned Poissant that changing times made it a bad line of work. Poissant scorned that advice—only to repeat it to his own son. "I keep telling him to stay away from this business because it's dying. Thirty years from now, all of this will be scrap yards and marinas. The piers used to be busier than hell. Now, they are ghost piers."

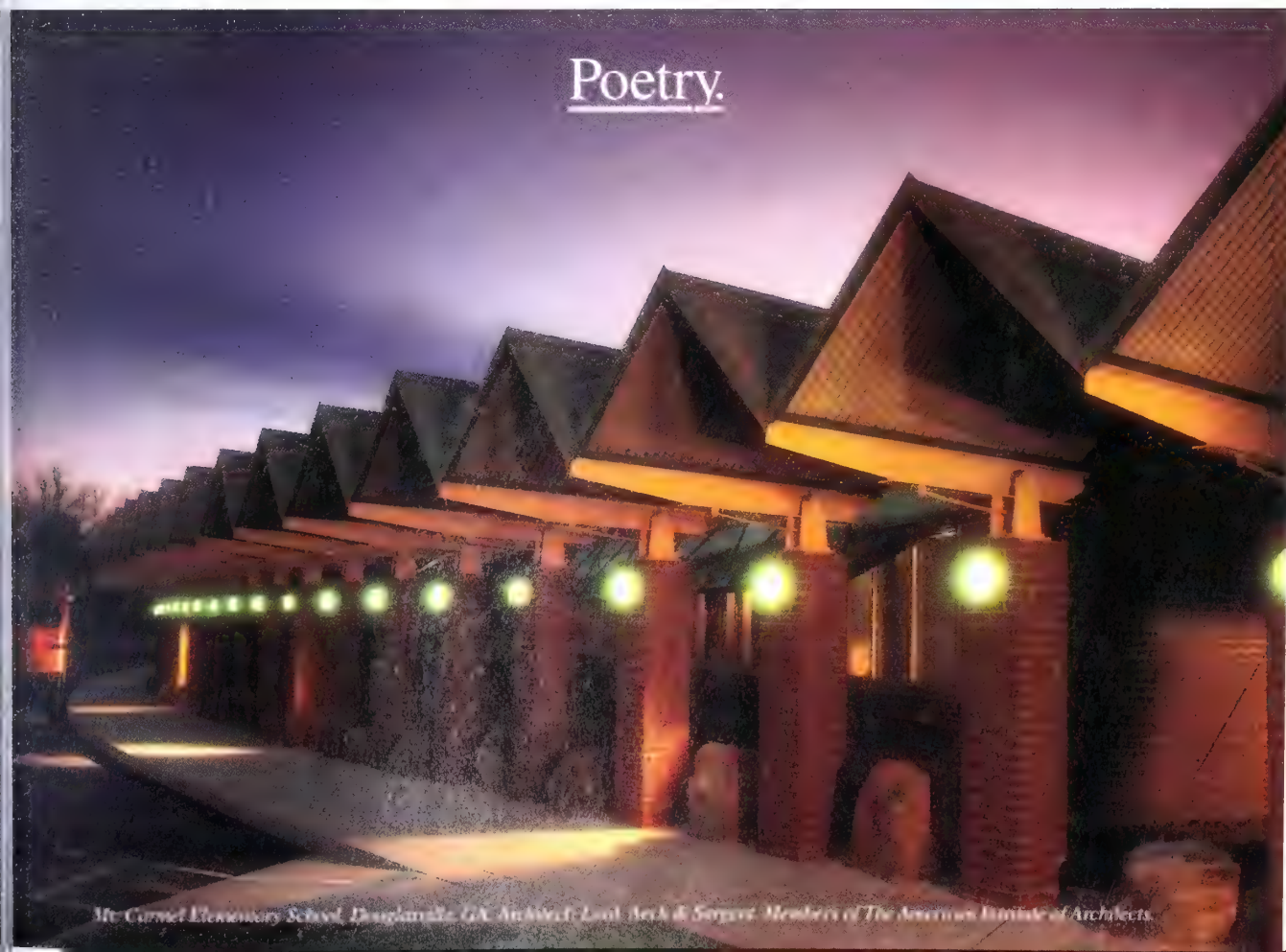
At 3 p.m., the Margaret Moran pauses in her rounds to drop me back off at the seawall at the Battery in Lower Manhattan where it had picked me up at 8 a.m. As I leave, I say goodbye to Christensen. "I don't know how much longer I will stay," he tells me in parting. "I will stay here until I can't do it anymore."

CINDY WEBB

*Webb was a BUSINESS WEEK summer intern.*

**URE** "We get jaded about it," says captain, as we ply past the Statue of Liberty, "but God, it's beautiful"

week to two-week gigs, says Poissant. Negotiations with the Greenwich (Conn.)-based tugboat line, which declines to comment. In the meantime, Poissant says he got so jaded on board that his wife's cooking didn't taste the same. His wife, he says, has been a very good sport about his work and adds that the new two-week schedule is a blessing, despite longer



Mt. Carmel Elementary School, Douglasville, GA. Architect: Louis Berk & Sonnet. Members of The American Institute of Architects.



## BOOK BRIEFS

### THE LAST HARVEST

The Genetic Gamble That Threatens to Destroy American Agriculture

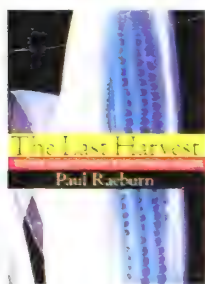
By Paul Raeburn

Simon & Schuster • 269pp • \$24

## GENE CALAMITY

For all its vast natural resources, North America lacks one crucial asset—the genetic gold of food crops. Of the world's top 20 crops, including wheat, corn, and rice, not one has wild ancestors in the U.S. Harvests in America “are powered by foreign genes just as surely as our industry is powered by foreign oil,” observes one expert quoted by Associated Press science writer Paul Raeburn in his provocative new book. What's more, the rest of the world isn't much better off.

That dependence brings the seeds of potential calamity, argues Raeburn. Food crops are constantly being threat-



ened by new pests or plagues, from the fungus that caused the 1846 Irish potato famine to the leaf blight that wiped out 15% of the U.S. corn harvest in 1970. That's why breeders must keep adding genetic material from other varieties—or from wild ancestors—that can fight off threats better.

The problem, Raeburn writes, is that “vital genetic resources are disappearing with virtually no notice.” For one thing, farmers in the U.S. and around the world are planting fewer crop varieties. Almost the entire U.S. potato harvest comes from just six types. In India, 30,000 traditional varieties of rice have been largely replaced with only 10.

Just as ominous may be the extinction of the wild relatives of crops. Raeburn recounts the exciting 1977 find of an uncultivated corn plant in Mexico. But he points out that it could easily have gone extinct before the discovery.

Theoretically, such genetic gems can be preserved in seed banks. But Raeburn finds that many are falling down on the job. And if the loss of genes continues, “America's and the world's agriculture must ultimately suffer catastrophic losses,” he concludes. “We will be unable to feed ourselves.”

It's a sobering tale, marred only occasionally by hype. Along the way, Raeburn provides fascinating historical nuggets. Thomas Jefferson smuggled rice seeds out of Italy, an offense then punishable by death. Intrepid plant hunter Frank Meyer crossed deserts and fought brigands in order to bring back 2,500 new plants to the U.S. early in this century. And Russian botanists chose to starve rather than eat up the genetic treasure in Leningrad's seed bank during World War II. If Raeburn is right, that's the kind of dedication we need now to prevent gene loss from eventually causing mass starvation.

BY JOHN CAREY

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BY JOHN CAREY

### CITY OF BITS

Space, Place, and the Infobahn

By William J. Mitchell

MIT Press • 225pp • \$20

## VIRTUAL DESIGN

What will be the architecture of cyberspace—our concept of the virtual worlds presented by advanced computer networks—and who will get to design it? How will those networks, with their ability to change our perceptions of space and extend our senses, alter our use and design of buildings and cities? Those are the kinds of questions William J. Mitchell addresses in *City of Bits*, a fascinating essay about how computer networks and the traditions of architecture and design are affecting each other.

Mitchell is versed in both fields. He has been surfing the Internet ever since its predecessor, called ARPANET, came to life 25 years ago. He delights in heralding the new institutions that technology is spawning: 24-hour electronic markets, virtual theaters, and all-electronic libraries. Yet as professor of architecture and media arts and sciences at Massachusetts Institute of Technology, he writes knowingly of how buildings, streets, and public spaces have historically shaped the patterns of daily life. And now, as technology changes the design of those places, he says, patterns of life are bound to change, too.

Winston Churchill once said that we make our buildings and our buildings make us. With refreshing wit and lucid writing, Mitchell succeeds in updating that aphorism for the computer age.

BY JOHN W. VERITY



### ONLY IN AMERICA

The Life and Crimes of Don King

By Jack Newfield

Morrow • 352pp • \$23

## LORD OF THE RING

Veteran New York journalist Jack Newfield's *Only In America* paints a convincing portrait of boxing promoter Don King as one of the most nefarious scalawags in American sports business. King, now 63, got his start in numbers racket in Cleveland. He spent four years in prison for kicking a man to death (though he later was pardoned, possibly as a political payoff). According to Newfield, King's morals improved only marginally in the intervening 24 years, as he clawed his way to the top in boxing promotion.



In Newfield's telling, King has a certain perverse attractiveness. He rose from a background of poverty and crime, using street smarts, malaprop-filled blarney, and hard work to bull his way in almost every major fight, starting with Muhammad Ali's epic 1974 bout with George Foreman. Along the way, King charmed—and usually outfoxed—everyone from TV executives to FBI agents.

But this book is mainly an exposé of King's alleged misdeeds. Citing letters and other documents and interviews with boxers, law enforcement agents, and ex-confidants of King, Newfield accuses the promoter of routinely ripping off fighters by skimming their purses and padding their expense tabs. King, Newfield says, also increased his take by packing fighters' entourages with members of his family. And then there's King's racial hypocrisy: He uses a black solidarity pitch to lure African American fighters away from white promoters only to squander their talent in demerol-fueled bouts against great-white-hope posers with TV appeal. Mike Tyson's April 1987 drubbing of Peter McNeeley is one of the most recent examples.

In the end, Newfield's case against King may try the patience of many readers. Long before you finish, you're left with two big questions: How could we have ever allowed such a man to dominate a major sport? And given the cynicism behind his matches, why do we anyone pay to watch them?

BY THANE PETERS



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**THE WINNER-TAKE-ALL SOCIETY**  
Robert H. Frank and Philip J. Cook  
Doubleday Press • 272pp • \$25

# IF YOU'RE NOT NO.1 YOU'RE ZERO

To the victor belong the spoils: That age-old adage seems to have become the motto of today's economy. When an actor earns \$20 million for one movie, nobody blinks. And the average weekly paycheck of a CEO comes to dwarf annual salaries earned on the shop floor.

Yet there's a spreading sense that something is awry: A widening gulf between the few haves and the many have-nots has contributed to political anger among U.S. voters. In sync with that mood, Robert H. Frank and Philip J. Cook, economics and public policy professors at Cornell and Duke Universities, respectively, try to identify the conditions that lead to global markets in which, increasingly, the bulk of the money goes to a few stars. Their book, *The Winner-Take-All Society*, also considers the implications for society when winning is far more important than how you play the game.

Winner-take-all markets have proliferated for many reasons, say Frank and Cook. Among the causes: Falling transportation costs, the spread of telecommunications, and the wider use of English as a common language have turned once-small regional markets into targets for global competition. The mass media have given a few entertainers and sports figures dominance. And intense competitive pressures drive corporate boards to spend big bucks for the "best" consulting firms and executives from other companies. In the 1960s, top corporate suits rarely switched employers: Now nobody is shocked when Louis Gerstner Jr. jumps from RJR Nabisco to IBM.

What's important in a winner-take-all market is not absolute performance but relative results. Being really good still not cut it: You have to be better—perceived as better—than all others to gain star status. Take Mary Lou Retton, the gymnast who took the Olympic gold in 1984. As the authors point out, "her endorsement contracts have earned her millions in the years since her medal. But although Retton's victory over the silver medalist came by only a slim margin, today almost no one can even remember the runner-up's name." (It was Romania's Ecaterina Szaba). Likewise, Microsoft's Bill Gates became a billionaire because his company's software lords it over the computer field.

Nor are human beings the only ones to compete in winner-take-all markets, say the authors. Technologies, nations, and novels vie for the top spot, too. For example, VHS overtook Betamax technology to become the primary way to view and record videos: No dealer nowadays would even attempt to sell a Beta VCR.

While some of this analysis is not new, Frank and Cook break ground by credibly linking the win-at-all-costs mentality to economic and cultural problems. Income inequality is the most obvious of these, but there are other issues. Among the winners are big conglomerates, which exacerbate social inequality and lower cultural standards by building markets around lowest-common-denominator products—ever-more-violent movies and dumbed-down news coverage, for example. (That doesn't mean niche markets are slighted: The authors describe a "countervailing" boutique movement, wherein large markets are transformed into several smaller ones, such as microbreweries and specialty clothing shops, but they feel this is often temporary and leads to a new round of consolidation.)

Winner-take-all markets also encour-

age bad career choices: On a large scale, this means a waste of economic resources. People tend naturally to overestimate their ability to become the next George Soros or Madonna, the authors report. One survey shows that 90% of today's workers feel they are more productive than the median worker. Many Americans, it seems, live in Garrison Keillor's mythical Lake Wobegon, "where all the women are strong, all the men are good-looking, and all the children above average." Combine that phenomenon with market incentives that lure too many "contestants" away from realistic job choices, and you have significant income loss and a much less productive economy.

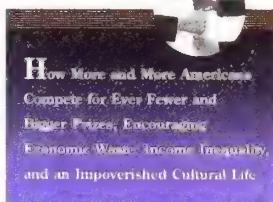
Then there's the growing elitism in higher education, perhaps the most disturbing consequence of the winner-take-all phenomenon. Of course, the Ivy League colleges have always enjoyed a stellar reputation, but today they and a few others have become the only destination of choice for the top students.

The authors show how America's most gifted young people flock to just 20 or so institutions. One example: In recent years, 59% of the high school seniors recognized by the Westinghouse Science Talent Search enrolled in just seven colleges, up by more than 10 percentage points from the 1970s. But of course, not everyone—not even all the highly gifted students in the U.S.—can attend the top 20 colleges.

Another big problem: Businesses, which once recruited at many universities, now concentrate their recruiting efforts on the same few. That leaves equally qualified job applicants out in the cold.

To enhance their reputations, universities even try to influence the media rankings used by students in deciding where to go, say Frank and Cook. Specifically, the authors suggest that some graduate schools try to skew *BUSINESS WEEK*'s ranking of the top-20 business schools to move up in the survey. The authors, however, give examples only of how the survey could be manipulated, such as assigning the best professors to the students they believe will be in the *BUSINESS WEEK* survey's cohort. But

## THE WINNER-TAKE-ALL SOCIETY



ROBERT H. FRANK PHILIP J. COOK

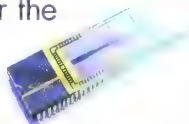
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## Books

they do not indict any specific school.

There are problems with the author's arguments. Maybe, they say, the economy would benefit if all those actor-writers hung up their ambitions to pursue other careers. But would the aspiring thespians be any happier? Would America be better off if Herman Melville's failure as a writer in his lifetime, if concentrated on his work at the U.S. Customs House rather than dreaming about the white whale? Besides, what would serve us *café latte*?

Still, the thesis is generally convincing. So if the mania to be No. 1 is so constructive, how do we curb it? Unfortunately, the book falls short on practical solutions. Frank and Cook say private not public—means should do the job of restricting individual behavior. For instance, as TV shows become more violent in quest of bigger audiences, pe-

**The winner-take-all  
phenomenon often  
results in poor use of  
economic resources**

ents—not government censors—could fight back with the "V-chip," which allows them to restrict their children's viewing. And to counter any tendency toward cheating in sports, there are societal pressures and rules that are self-enforced by sports leagues.

But the authors' other solutions depend on government action. To rebalance income distribution and penalize people for ostentatious spending habits, Frank and Cook would replace the current income-tax system with a consumption tax. And they argue that legislative tort reform and changes in health-care financing would curb the incomes of lawyers and doctors and make these occupations less desirable.

The popularity of television shows such as *Law & Order* and *ER*, however, suggests that Americans are intrigued by those professions even when represented by poorly paid district attorneys and hospital residents. And changing tax laws won't stop Bobby Bonilla from nabes from working on their hitting instead of their homework. Hey, not even basketball star Michael Jordan could resist that siren song.

BY KATHLEEN MADIGAN

*Madigan tracks the economy's winners and losers in BUSINESS WEEK's Business Outlook column.*

**"... East is East, and West is West,  
and never the twain shall meet..."**

**Rudyard Kipling**



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The image is a full-page advertisement. The top half shows a sunset with a bright orange and yellow glow on the horizon, transitioning into a deep purple and blue sky. The bottom half of the image is a dark, almost black, silhouetted foreground, possibly a field or a body of water, which is mostly obscured by the text. The text is positioned in the upper left quadrant, with 'This' in a small font, 'unobstructed' in a large, bold, sans-serif font, and 'view brought to you by new Microsoft Office' in a smaller font below it.

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BY STEPHEN H. WILDSTROM

## PRICE WARS POWER UP QUALITY

In the early days of personal computers, it was depressingly common to pull a brand-new computer out of a box, set it up, turn on the switch—and see absolutely nothing happen. It's been several years since I've seen a dead-on-arrival machine. The rash of failures that used to plague PCs—from crashing hard disks to dying keyboards—have all but disappeared.

Remarkably, the improvement in hardware quality has come during an unrelenting price war that has kept manufacturers under a constant cost squeeze. In the fiscal year ended last January, for example, Dell Computer Corp.'s operating margin was a slim 7%. But far from prompting manufacturers to cut corners, the pressure is forcing them to get it right the first time and save money on returns and technical support calls. "It's a lesson the Japanese taught us," says Webb McKinney, general manager of Hewlett-Packard Co.'s home-products division. "Quality results in lower total cost."

**SMALLER CHIPS.** In short, the price wars have brought about more than just lower prices. Improvements in quality are likely to continue, thanks in large part to better technology. Ever smaller, more powerful chips are an example. A five-year-old network interface card I found in my office contained 39 chips. The entire system board of a new Macintosh Performa 5200 carries just 19.

Fewer components means fewer points of potential failure and less chance of errors in assembly. "There's a direct correlation between simplicity and quality," says Rick Smith, director of quality for Compaq Computer Corp.'s desktop operations.

Factors as mundane as soldering technology affect cost and quality. Early circuit boards were made by inserting components through holes, and the solder joints were prone to weaken or



short-circuit. Now, automated machinery solders the chips directly onto metal traces on the board, a method that is both cheaper and more reliable. Intel supplies some new Pentium chips on spools of film that can be bonded directly to circuit boards by ultra-precise assembly machines. "Our industry has moved faster than most," says Mal D. Ransom, vice-president for marketing at Packard Bell. "We've done in five years what took the auto industry 50."

Manufacturers report that

returns due to defects have become rare. Acer America Corp., which sells its machines mainly through mass-market retailers, gets about 5% of them back, but inspection shows no defects in the overwhelming majority. Steve Garcia, product manager for Acer, speculates that most of the machines are returned because customers found a better deal at another retailer or they simply changed their minds. Dell, which sells directly to generally more sophisticated customers, reports only about 1% returns for all causes.

**SOFTWARE SLIPS.** Of course, computers have room for improvement. The biggest area for further quality improvement is disk drives. Unlike solid-state chips, mechanical devices wear with age and disk drives remain the most trouble-prone component. Another area ripe for improvement is product support and advice. Judging from the grumbling I hear from readers, it's harder than it should be to get help over the phone, and getting a broken machine fixed is worse.

Even so, the whole quality picture for computers is better than in the much more profitable software industry. It's the only business I know of where manufacturers routinely sell products they know to be defective—and customers accept "We'll fix it in the next release" as a response. Windows 95, for example, was shipped out with dozens of glitches that won't be fixed until a November "tune up." It's too bad that consumers can't expect their software to work as reliably as the hardware it runs on. Then the personal computer would be a lot closer to what many industry executives say, with some hyperbole, is their goal: A product that's as easy to use as a toaster.

## BULLETIN BOARD

### HARDWARE

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With a slew of excellent, inexpensive color printers crowding the market, manufacturers are turning to software to make their products stand out. Canon Computer System Inc. (800 848-4123) is making its fall line of ink-jets into



arts-and-crafts machines. The \$250 BJC-210, \$350 BJC 4100, and \$550 BJC-610 come with Windows software to produce greeting cards, stationery, colored stickers, and needlepoint patterns. You can also print on fabric or create iron-on transfers.

### SOFTWARE

#### NEWS FLASH

Business Wire, a distributor of corporate announcements and news releases, has a new delivery system. For \$14.95 a month, it will give you a private page on its World Wide Web server. Just specify the information you want to see on what classes of companies. Then retrieve the information with Netscape or any Web browser. Brief summaries of releases appear on your Web page, sorted by category with the full text available by clicking on the headline. For more information, check <http://www.hnt.com/bizwire>.



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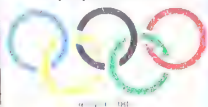
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BY GARY S. BECKER

## HOW TO SCUTTLE OVERFISHING? TAX THE CATCH



**NO QUOTAS:**  
Limiting the  
total take just  
encourages a  
rush out to  
sea. A tax  
system would  
spread fishing  
over the  
season and  
raise funds

As a summer resident of Cape Cod, the Massachusetts seashore, I realize that the importance of fishing for food, livelihood, and sport may be a bit out of proportion there. But the local debate on controls over the striped bass—called stripers, a delectable white fish and longtime staple of gastronomes on the Cape—is a concrete example of the general issue of obstacles to intelligent regulation.

In the 1970s, the stock of striped bass in ocean waters offshore from Maine to Maryland became seriously depleted because of a combination of droughts, pollution in breeding grounds, and overfishing. In response, Massachusetts and other states in the region established strict quotas for commercial and recreational fishing. Overfishing may not have been the main reason for the dwindling supply, but environmentalists made a persuasive case that restrictions on fishing could help restore the stock.

Massachusetts placed a ceiling on the aggregate catch of stripers by commercial fishers. Unfortunately, this is a very poor way to control fishing, because it encourages each fishing boat to catch as much as it can early in the season, before other boats bring in enough fish to reach the aggregate quota that applies to all of them.

**"FISHLESS WEEKS."** This is precisely what happened last year, when the Massachusetts commercial quota of 200,000 pounds was already reached by the end of July, well before the normal finish to the fishing season in September. The rush to catch stripers early sharply lowered the wholesale price while fishermen had a lot to sell. The price then increased steeply, after the quota was exhausted and not much striper was on the market. The perverse incentives provided by the quota added to the difficulties of making a living from fishing in this region.

The number of striped bass in the waters off the coast has grown rapidly in recent years—perhaps because the controls over fishing helped in the breeding of additional stock—so Massachusetts increased the commercial allowance to 750,000 pounds in 1995, nearly four times the 1994 level. Because even this larger quota was expected to be reached early, the state tried to spread out the catch over the season by prohibiting commercial fishing for stripers during "fishless weeks" for stripers. As a result, fresh striper

has been both expensive and scarce during these weeks.

A much better way to regulate fishing is through quotas and fishless weeks—and one that should appeal to consumers, fishermen, sportsmen, and taxpayers alike—is for the states to tax the amount of fish caught. The tax would vary by weight and size, so that catching excessively small and young fish could be penalized severely. The present rules require stripers below a minimum size to be thrown back **ONE A DAY.** The size of the tax would control the total catch, because fishing for stripers would decrease when the tax rate is high. This approach eliminates the incentive under the present system to catch fish early in the season, since fishermen who are taxed on their catch have no reason to attempt to bring in stripers before competitors do. Instead, they would spread their fishing over the season and try to catch more fish when prices are higher.

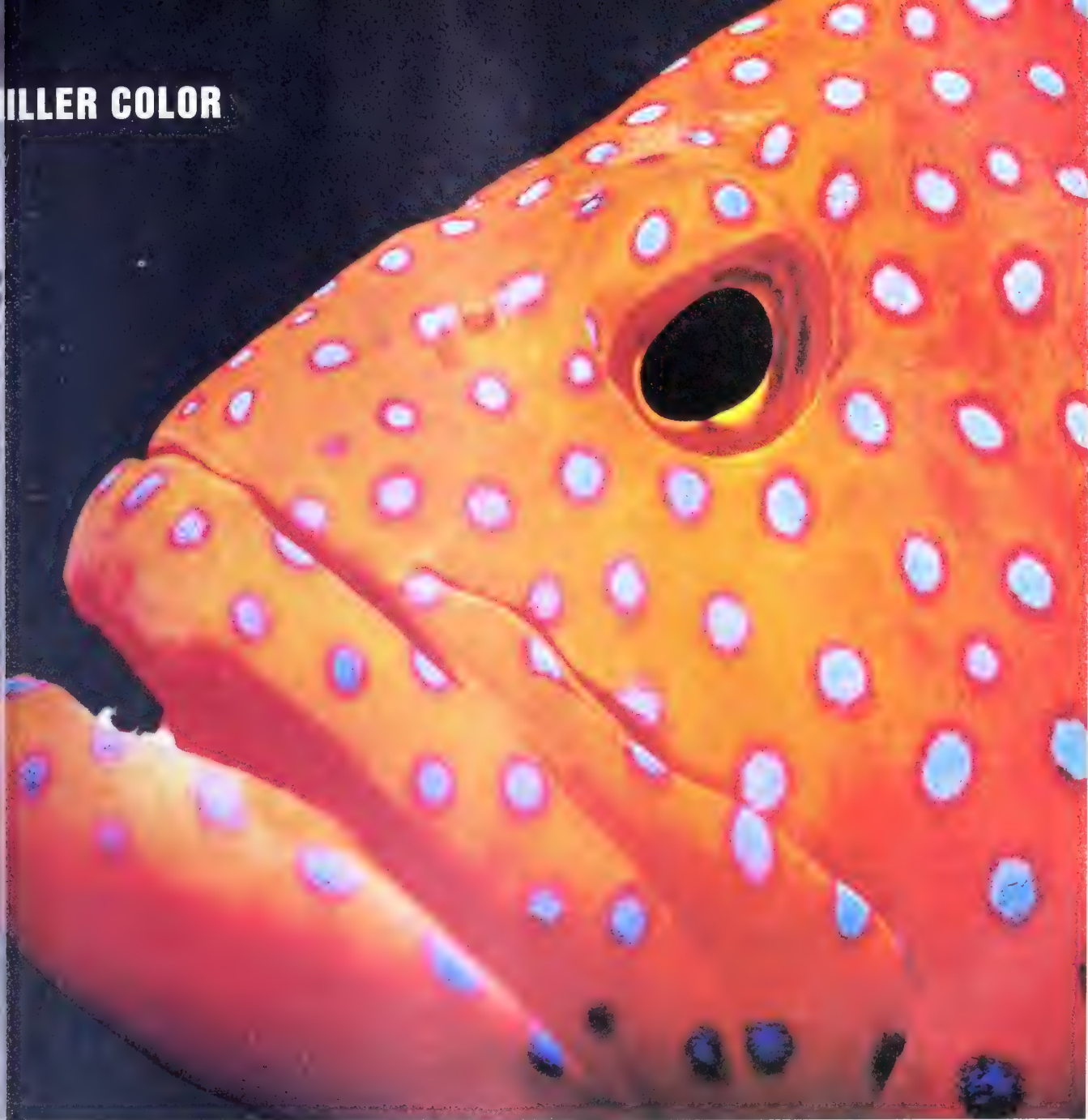
Recreational fishermen may be responsible for more than half the total stripers caught, which is why they too are regulated. Massachusetts presently allows each person fishing to catch one striper per day. The same tax rate should apply to both commercial and recreational fishing, since the effect on the stock of stripers in the sea is no different when fish are caught by one group or the other.

A system of taxes on fish caught by commercial and for-hire recreational fishing boats is no harder to implement than monitoring the catch, as required by the present quota system. A tax has the further advantage of providing additional state revenues, which could be used to fund research on the causes of the large and disturbing fluctuations in the stock of striped bass and other fish and to find ways of improving the marine environment.

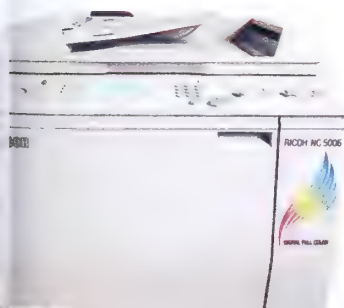
It is not easy to enact sensible controls even in a small-scale industry such as fishing for striped bass, where the case for regulation is rather strong. One must wonder about what happens in the larger political arena when the advantages of regulation are questionable, especially in large national industries with lots of media attention. This may be particularly pertinent to current disputes over general environmental regulations and deregulation with regard to health and safety issues. This is the main lesson about regulation from the big fish story on the Cape.

Gary S. Becker, the 1992 Nobel laureate, teaches at the University of Chicago and is a Fellow of the Hoover Institution.

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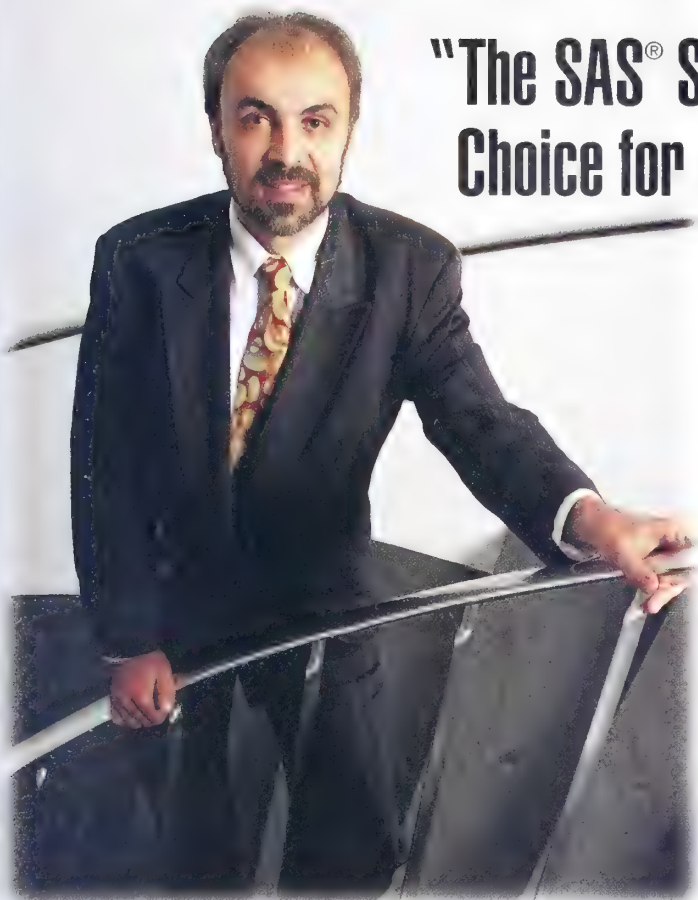
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The kit contains a prospectus with more complete information on the 1% redemption fee, advisory fees, distribution charges, and other expenses. Please read it carefully before investing or sending money. © Vanguard Marketing Corp., Distributor.

IMPORTANT INFORMATION FOR INVESTORS: A subscription period for Vanguard Horizon Fund is scheduled to begin on June 30, 1995, and end on August 14, 1995. During this period, purchases by check or wire will be invested in money market instruments to allow the Portfolios to accumulate sufficient assets for investment beginning August 14, 1995. Written exchange requests out of other Vanguard Portfolios into the new Vanguard Horizon Fund received during the subscription period will be executed at the end of the subscription period on August 14, 1995.

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Moser contends that using the SAS System has also turned traditional developer/end user wars into "a cooperative process. Now they sit side by side, building the application together." And saving the bank both time and money.

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SAS System as the tool for turning their data into meaningful information, UBS financial analysts can be certain those decisions are based on the most comprehensive, up-to-date information available.

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**The Union Bank of Switzerland** is the largest bank in Switzerland. Core to the bank's success is its reputation for personalized customer service among large investors. *Providing* that service is the job of UBS' team of investment research analysts, who support portfolio managers and investment advisors in determining what to buy, what to sell, and when.

They're finding answers in the SAS System, which enables over 70 financial analysts to advise portfolio managers on the best portfolio mix. "Our strategy is to find ways to enable analysts and financial advisors to handle information more easily and quickly," says UBS Vice President Beat Moser. "What that meant was finding a software tool that could eliminate the redundancy of information and time caused by the use of several different analysis products—each limited in terms of functionality and ability to access key data. And it meant finding a tool that allowed applications to be developed, and changed, fast."

**Smart Move, Smart Money** Moser believes that UBS has resolved those challenges in their choice of the SAS System as their strategic software. "Our previous system required many labor-intensive steps as data was moved from one software product to another," recalls Moser. "Today data access, management, and summarization is handled automatically by the SAS System. This has given us productivity gains of up to 200% in some areas. The SAS System is fully integrated and meets most of our analysis needs—it's our strategic choice in various research units of our bank."

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**Executive Summary**



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BY MICHAEL J. MANDEL

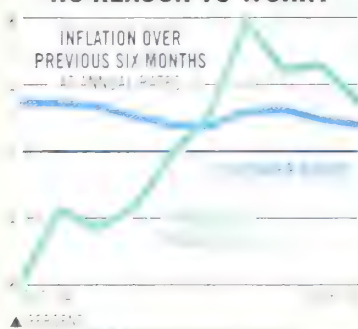
## LEAKS IN THE 'PIPELINE' THEORY

A new look at how inflation works

For inflation-wary Wall Street economists, the sudden rise in commodity prices in late 1994 and early 1995 was a sign of impending consumer-price inflation. The talk back then was that a rise in the price of raw materials would inexorably travel down the "inflation pipeline," forcing companies to raise prices for the goods they sold.

But a new study from economist Todd E. Clark at the Federal Reserve Bank of Kansas City casts some doubt on the pipeline theory. He found that the crude-materials producer-price index can often soar or plummet without affecting consumer prices. Costs of raw materials, for instance, rose sharply in 1987 without greatly pushing up consumer inflation.

### NO REASON TO WORRY



The pipeline theory breaks down, Clark argues, because prices of consumer goods depend more on productivity and labor costs than on raw materials. In today's corporate environment—with productivity rising, wages flat or falling, and health-care costs moderating—companies can earn good profits without raising prices. Indeed, intense competition may even force companies to lower their prices.

That may well be the reason why, despite the increase in raw-material prices that occurred earlier this year, the inflation rate for American consumer goods has been falling (chart). How low can it go? Edward E. Yardeni, chief economist at Deutsche Morgan Grenfell/C.J. Lawrence, thinks that the overall consumer-inflation rate could fall as far as 1.5% in 1996.

## THE ECONOMICS OF AIDS

Its impact may be less than feared

By any measure, the AIDS epidemic is wreaking terrible havoc on a global scale. Current estimates project that, by 2000, some 30 million to 40 million people throughout the world will be infected with HIV, the virus that causes AIDS.

But the personal and social tragedy aside, AIDS may have less of an economic impact than feared, according to a new report by David E. Bloom and Ajay S. Mahal of the National Bureau of Economic Research. Development experts originally worried that the AIDS epidemic would reduce economic growth in such hard-hit African nations as Tanzania and Malawi. AIDS was thought to be more common among highly skilled urban workers, the backbone of any economic development effort. And high medical costs for AIDS patients were going to drain needed funds away from economic investment.

In comparing countries with high and low levels of AIDS, however, Bloom and Mahal find no evidence that per capita income grew more slowly in the former group. One reason: Many developing countries have enough surplus labor to make up for the AIDS-related losses. Moreover, more highly educated workers seem to be taking measures to protect themselves.

Despite these results, Bloom and Mahal observe that the AIDS epidemic may do serious economic damage to particularly hard-hit geographic and demographic groups. In any case, the human toll of AIDS cannot be assessed in mere economic terms.

## A BLEAK FUTURE FOR PC REPAIR

The job boom probably won't last

When cars became available to the average American, they created a whole new specialty: the auto mechanic. The industry now employs more than 500,000 workers.

Similarly, today's boom in home computers leads some experts to suggest that computer repair will be the hot occupation for the second half of the 1990s. The Bureau of Labor Statistics projects a substantial increase in the number of computer-repair technicians

over the next decade. Indeed, after several years of decline, the number of repair technicians for computers and other electronic gear took a leap upward in 1994 (chart).

But a report from Dataquest Inc. casts doubt on the future of this boom. By its estimate, spending on hardware maintenance and support will slow sharply late in the coming decade, from an annual growth rate of 8.8% in 1994-97 down to only 2.1% growth in 1997-99. The spending on hardware maintenance for desktop computers will actually fall, as the products become cheaper and more reliable, making on-site service less necessary (page 26). "There's not a lot of profitability in service," says Clyde Nibors, executive director of the International Society of Certified Electronics Technicians. "It's a high-expense, low-dollar-value business."

Instead, computer makers are hiring large numbers of telephone support people, who talk customers through their hardware and software problems. "Over 80% of our calls turn into a call where we need to send out a replacement part," says Jim Collas, vice-president for customer support at Gateway 2000. As befits the age of communication, the key tool for computer repair now seems to be the telephone rather than the soldering iron.

### TEMPORARY UPTICK?



## THE HARD-HIT U.S. WORKER

Wages' share of the pie drops again

The latest figures from the Commerce Dept. confirm what most people already knew: Workers are still taking it on the chin. According to a report released on Aug. 30, the share of national income that is devoted to wages inched down again in the second quarter of 1995, hitting 59.8%, which is a new postwar low.

The wage share has now fallen for five straight quarters. And benefits are not making up the slack, either: The share of national income is flat over the past year.

# SPOTLIGHT ON BOOKS

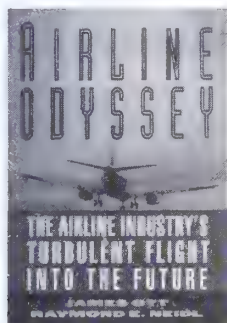
Three new titles BusinessWeek readers won't want to miss

by Mark G. Graham

## AIRLINE ODYSSEY

The Airline Industry's Turbulent Flight into the Future

by James Ott and Raymond E. Neidl  
McGraw-Hill, 252 pages, \$24.95



Over the last five years, the world airline industry has endured more upheaval than in any other comparable period of the post-world war era." So write long-time industry observers James Ott and Raymond E. Neidl in their incisive new book *Airline Odyssey*. Drawing on hundreds of interviews with airline, aerospace and government officials, the authors offer a far-ranging, behind-the-scenes look at a \$203 billion industry that is still reeling from the United States government's 1978 decision to deregulate domestic airlines. It's a brave new world of corporate battles, dramatic upheavals and pivotal personalities that will continue to shape the airline industry well into the 21st century.

*Airline Odyssey* analyzes why such once profitable carriers as Eastern and Pan American really failed, and which airlines may be doomed to follow in their footsteps. It features in-depth portraits of the Big Three—American, Delta and United—and shows how low fares are threatening their future profitability. Ott and Neidl also provide dramatic details of United's employee takeover, and examine spiraling labor costs, rapid over-expansion, rising fuel prices, and the uncertain future of frequent flyer programs.

Thankfully, this is not just a tale of mismanagement and failures. Here, too, are the triumphs—like the Cinderella success story of Southwest Airlines. Southwest has become what the authors call the "avatar of the new domestic carrier," succeeding when its owners recognized its niche market and exploited it. The book also offers insight into the groundbreaking partnership of KLM Royal Dutch Airlines and Northwest.

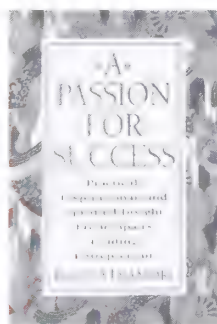
Hailed as "the world's most advanced alliance," the KLM-Northwest marriage may be, according to Ott and Neidl, the shape of things to come and one key to the revitalization of the airline industry.

*Airline Odyssey* is well-researched and engagingly written. And although it has been obviously penned for the general public, investors interested in long-term trends will also want to give it a read. "The past is prologue," writes Ott and Neidl in these pages. "The upheavals of the last five years are just a taste of what lies in store." For the moment, however, it remains to be seen whether the international airline industry will be able to adapt ... or go the way of the dinosaurs.

## A PASSION FOR SUCCESS

Practical, Inspirational, and Spiritual Insight From Japan's Leading Entrepreneur

by Dr. Kazuo Inamori  
McGraw-Hill, 192 pages, \$16.95



Dr. Kazuo Inamori is no stranger to success. He is the founder and chairman of Kyocera Corporation which he founded in 1959, with only \$10,000. Today, this \$5.76 billion company is on the leading edge of technology, producing everything from high-tech ceramics to wireless telecommunication services. Despite his dazzling economic accomplishments, Dr. Inamori—twice-named Japan's most effective manager—does not believe that the single-minded pursuit of profit is the best way to run a business. Now this visionary entrepreneur shares his philosophy in his new book. Like the best-selling *Tao of Leadership*, this book fuses spiritual and inspirational ethics with a practical business sensibility. Each page contains one central thought, an aphorism if you will, that encapsulates one of Dr. Inamori's

key principles for success in both your business and your personal life.

The book's first section—"How to Succeed in Life"—looks at finding a purpose in life, being realistic about both your talents and your limitations, and learning from the wisdom of those more experienced than you.

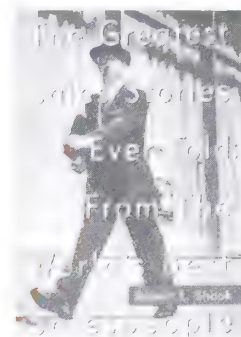
The second half of *A Passion For Success* is devoted to "How to Succeed in Business." He offers advice on making the right decisions, developing a mindset that attracts profitability and overcoming the fear of failure.

*A Passion For Success* by Kazuo Inamori is a deeply personal and heartfelt book. It's for every business professional who wants to enhance his or her work as they navigate the often perplexing and confusing corporate maze.

## THE GREATEST SALES STORIES EVER TOLD

From The World's Best Salespeople

by Dr. Robert L. Shook  
McGraw-Hill, 250 pages, \$18.95

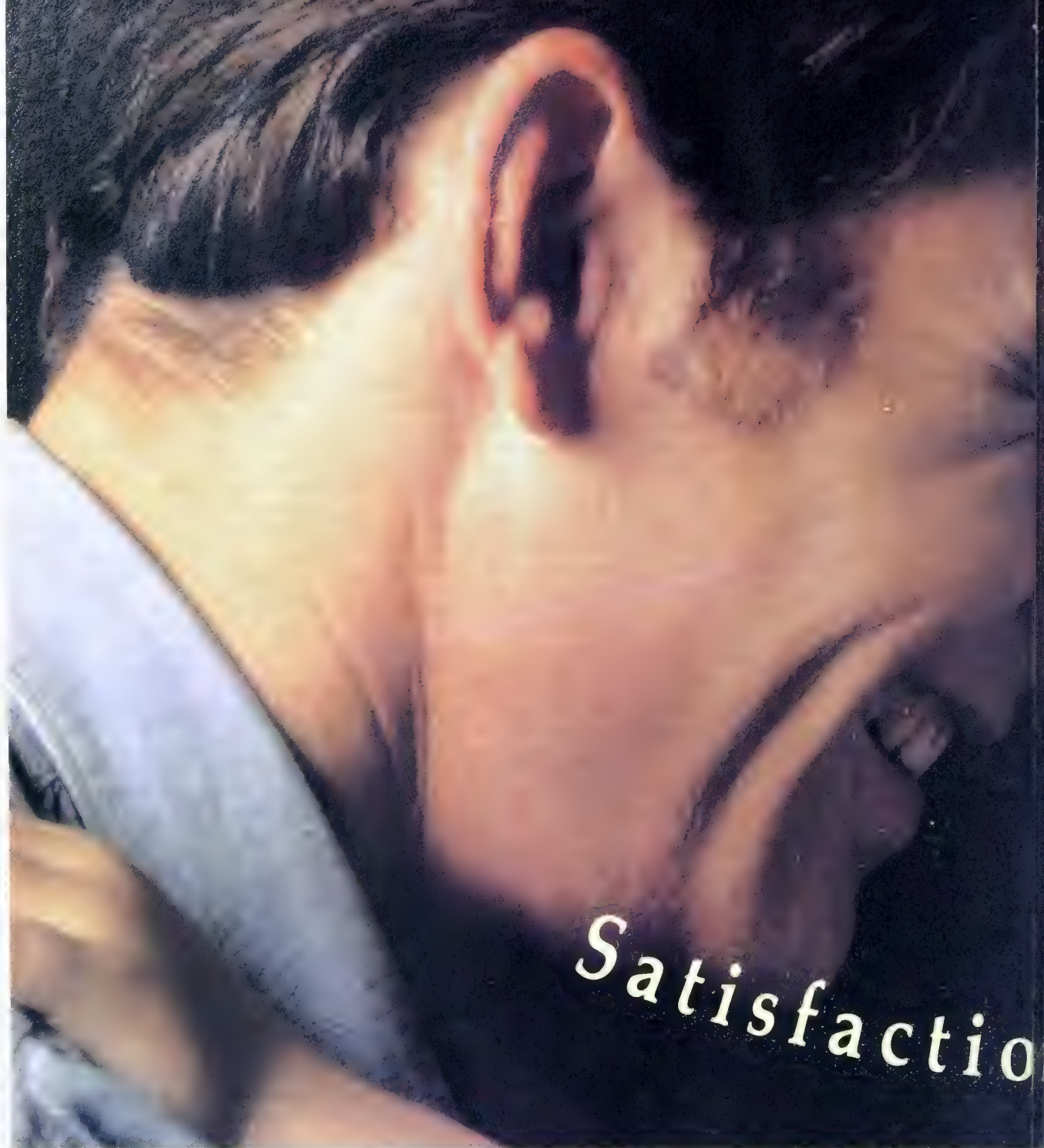


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JAMES C. COOPER & KATHLEEN MADIGAN

## THE JUMBLED NUMBERS STILL ADD UP TO A SOFT LANDING

**U.S. ECONOMY** On the day many Americans left work early to start the Labor Day weekend, the government released its monthly look on the labor markets. But those who stayed in the office to examine the data in hopes of finding a clear sign of the direction of the economy and monetary policy should have gone on and left with everyone else. The August report was a mixed bag. Nonfarm payrolls increased by a robust 249,000, but the gain was not broad, and the July increase was revised sharply lower. The unemployment rate dipped from 5.7% in July back to 5.6%—its June reading—but the nonfarm workweek was cut, and hourly wages fell.

Other data also give conflicting views. The nation's purchasers said industrial activity declined in August, and the government's composite index of leading indicators fell 0.2% in July. Consumer spending was flat in July, but auto makers reported healthy sales gains in August. Construction in July remained upbeat, led by a rebound in housing.

Confused? Don't be. Taken together, the recent data show that the economy remains on its soft-landing path of slow growth and little inflation. For one thing, overall hours worked are rising this quarter at a pace that suggests economic growth of about 2% (chart). So, none of the numbers preclude an interest-rate cut at the Federal Reserve's meeting on Sept. 26.

**POLICYMAKERS** meeting at Jackson Hole, Wyo., gave the clue to their thinking. The Sept. 1-2 confab of Fed officials, academics, and Fed-watchers concentrated on fiscal policy and government debt, although Fed Chairman Alan Greenspan cited an academic paper recommending caution in cutting rates while Congress and the White House work out cuts in the budget deficit. That suggests the Fed will want to wait for the final 1996 budget before easing again.

But the budget may not be resolved for months, and most Fed policymakers believe monetary conditions already are restrictive. The data give the Fed the leeway to take another quarter-point baby step later this month to ensure that the expansion stays on track.

Some insurance may be needed because August job growth was not as strong as the top-line number suggested. More than 70,000 of the new jobs were in gov-

ernment, the result of more school districts starting classes in August rather than September. Temporary help, which had flattened out in the previous three months, jumped by 44,000.

Job growth is slowing down in 1995. Since March, an average of 113,000 jobs have been added monthly, down from 269,000 in the previous six months.

Moreover, the nonfarm workweek fell 12 minutes in August, to 34.4 hours. Most of the decline could be traced to a 24-minute drop in the workweek for utility workers, however, as the return to more seasonal weather after July's heat wave reduced overtime. The workweek could bounce back in September.

**THE BEST NEWS** was a turnaround in factory payrolls. Factory jobs managed a tiny gain of 12,000 in August, but it was the first increase in five months. And the factory workweek rose 12 minutes, to 41.5 hours, with longer overtime. That gain, plus the rise in payrolls, suggests that the worst may be over for manufacturers and that factory output probably increased in August.

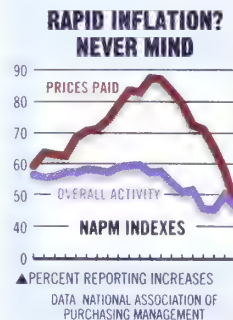
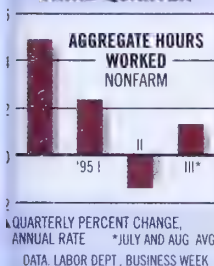
But while the August job report was saying positive things about manufacturing, the National Association of Purchasing Management told a grimmer tale. The NAPM's index fell to 46.9% in August, from 50.5% in July. The August reading was below 50%, suggesting industry contracted last month.

All the major components—employment, orders, production, and inventories—fell, but the decline in new demand was severe. The orders index slid to 46%, from 53.3% in July. The decline was split between falling domestic and foreign demand. One undisputed positive sign for the economy was the NAPM's price index. Prices paid for materials soared in the first half, but purchasers now report some price reductions (chart).

Still, any weakness on the production side of the economy is not as important as the performance of the demand side. So far this quarter, consumer spending and incomes still look healthy, as does housing. Demand for new offices and industrial parks is leading a resurgence in business construction.

After ending the second quarter on a high note, consumers began the third quarter with less vigor. Con-

### A SIGN OF A BETTER THIRD QUARTER





sumer outlays for goods and services, adjusted for inflation, were flat in July, compared with June. They surged 1% in May, followed by a 0.4% advance in June. Durable goods accounted for July's sluggishness, with a drop-off in car-buying contributing almost all of the weakness.

**EVEN THOUGH IT BEGAN MEEKLY**, however, don't expect third-quarter spending to stay puny. Because outlays were on the rise at the end of last quarter, they already show a 2.7% annual rate of growth, compared with the second-quarter average.

And August buying should bounce back, if only because car sales recovered. Sales of cars and light trucks, both domestic and imported, had fallen to an annual rate of 13.7 million, from 14.7 million in June, but August sales jumped sharply to 15.7 million.

Income growth looks strong enough to support solid spending gains. Personal income rose a strong 0.7% in July, reflecting strength in the key wages-and-salaries component. Adjusted for inflation and taxes, real disposable earnings rose 0.4%, starting the quarter at a 3.7% annual rate of growth from the second.

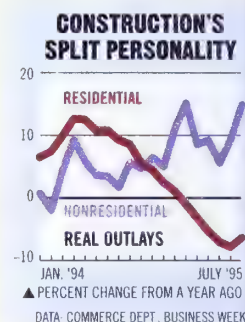
Despite the 0.2% decline in the average hourly wage rate in August, a clear trend toward slightly faster wage growth is now emerging. During the past three months, hourly earnings have grown 3% from the same period a year ago. That's up about half a percentage

point, compared with this time last year. Hourly earnings are now starting to keep up with inflation, after lagging far behind for more than a decade.

Better earnings and lower interest rates have combined to lift housing demand this summer. Residential construction was a big downer last quarter, but now seems to be turning around. Inflation-adjusted construction spending in the private sector soared 2.2% in July, lifting outlays well above their second-quarter level. Real residential building increased 1.6%, while business construction jumped 3.5%.

Housing is now ready to reinforce the gains in business construction, which is galloping along at a 15% annual pace (chart). During the past year, building of offices, motels, and other commercial structures is up 20%, as vacancy rates have fallen. Building of industrial plants and warehouses has also risen 20%.

By and large, the sectors that were the biggest drags on growth in the first half—housing, exports, and inventories—appear to be looking brighter in the second half. And while it's not yet clear from the data, the expansion is now on better footing.



## CANADA

### A LOT IS RIDING ON THE WILD CARD: QUEBEC

Canada took another step toward recession last quarter. But while growth will remain sluggish in the second half, an outright downturn seems unlikely.

Real gross domestic product fell 1% in the second quarter—its first drop in four years—after first-quarter growth of only 0.9%. Earlier interest-rate hikes in defense of the Canadian dollar, totaling 2½ points, slammed housing and consumer durables. Slower U.S. growth hurt exports, especially of autos.

The good news is that the drags from higher rates and weaker exports are lifting. The Bank of Canada (BOC) trimmed its overnight lending rate on Aug. 28 by a quarter point, to a range of

6% to 6½%, bringing total cuts since May to 1½ points. Also, the U.S. economy is picking up after its first-half slowdown.

However, paring of excess inventories, plus budget cutting, both federally and in the provinces, most notably Ontario, will keep growth subdued. Finance Minister Paul Martin on Sept. 1 pledged to cut the federal deficit to 3% of GDP by 1997, "come hell or high water," even if the economy is weak.

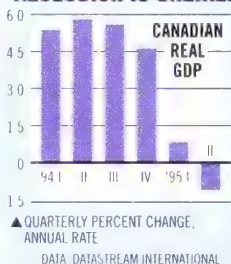
Fiscal optimism and less concern over Quebec's separatist movement have strengthened Canada's dollar by 5.5% vs. the greenback since January. Quebec is the outlook's wild card. Its gov-

ernment is proceeding with plans to hold a "sovereignty" referendum this fall. Recent polls suggest that it might fail, but any pickup in support would spook the financial markets.

As long as a "no" vote seems likely, a good inflation outlook also gives the BOC room to cut rates. Consumer prices were flat in June and July, as annual inflation dipped to 2.5%. Weak consumer demand, amid stagnant labor markets where joblessness is near 10%, is forcing retail discounting, and wage pressures are nil.

Given these market supports, investors are snapping up high-yielding Canadian bonds. The spread on 10-year Canadian and U.S. government bonds favors Canada by about 1½ points. And a failure of the sovereignty vote would be a big shot in the arm.

#### GROWTH FADES, BUT RECESSION IS UNLIKELY





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***C**lean, economical natural gas. Think what we'll save*



## CONGRESS



# BACK TO THE TRENCHES

## Business stands to win big in Congress

**A**s Congress launches into the final, frenetic months of the legislative session, Republican leaders still are trumpeting the rhetoric of radical reform. "This will not be an autumn of compromise," says Senate Majority Leader Bob Dole. "This fall, we will win our fight for revolutionary change, vote by vote and bill by bill."

Despite this political chest-thumping, the GOP has had to retreat from much of its original promise of wholesale change. But in America's boardrooms, the thrill of victory outweighs the agony over a few GOP defeats. Far from moping about the dwindling prospects for some key items of the Republican Contract With America, most

CEOs feel that the 104th Congress represents a milestone for business: Never before have so many goodies been showered so enthusiastically on America's entrepreneurs.

By yearend, Republican firebrands could deliver on some of business' top priorities. Congress will consider a budget plan, for one, that would wipe out the deficit over seven years. Business also sees hope for passage of a cut in the capital-gains tax and some relief from overzealous regulators.

Executives won't get all they have been pining for. House Republican radicals returning from summer recess are finding that moderate Senate Republicans—often allied with Democrats—are watering down the

conservatives' agenda. President Clinton is waving his veto pen to force more concessions. And Senator Bill Packwood's decision to fight an Ethics Committee recommendation to expel him for sexual misconduct poses another complication. Most key items of the GOP agenda must pass through the Finance Committee, which the Oregon Republican chairs.

Some business leaders also worry that hot-button social issues are diverting lawmakers from economic matters. "They better put some money on the bottom line," says T.J. Rodgers, CEO of Cypress Semiconductor Corp. "I

## THE REPUBLICAN REVOLUTION?

*Handicapping Congress' chances of passing bills important to business*

### TAX CUTS

**SUCCESS** \$200 billion in cuts, including capital-gains, family tax relief, and expanded IRAs.

**FAILURE** A modest, Clintonesque cut of around \$100 billion with no significant breaks for business investment.

**OUTLOOK** Success.

### BUDGET CUTS

**SUCCESS** Scrapping outmoded government programs. Example: Eliminating farm supports and the National Endowment for the Arts, privatizing the FAA's air-traffic control system. Deep Medicare cuts.

**FAILURE** Moderate cuts leaving a sizable budget deficit.

**OUTLOOK** Probable failure.





is other stuff—like griping about immigrants— isn't going to cut it."

Even if conservative Republicans lose me, though, corporate interests believe that by shifting the debate to the st way of reining in Washington, the P already has guaranteed that business will be a winner. "Clearly, dramatic change has occurred already," says John W. Snow, CEO of CSX Corp. "The mood in Washington is fundamentally different from the mood a year ago."

As the battle progresses, issues that matter to business will draw plenty of partisan fire, obscuring signs of the revolution's true progress. These key skirmishes will be critical if Republicans are to turn up winners:

**BALANCING THE BUDGET.** House and Senate Republicans have passed different budget plans that would kill off the deficit in 2002 by slashing more than \$1 trillion from projected federal spending. The key is finding a way to curb entitlements, such as Medicare, as well as scrapping entire areas of government largesse—farm subsidies, for example. "They have to eliminate whole programs. Otherwise, they will balloon again," warns William A. Niskanen Jr., president of the libertarian Cato Institute. Despite early GOP avowals to kill Cabinet departments, Republicans

have not eliminated any. Corporate subsidies, such as Agriculture's export-promotion program, are intact. Even pet targets, such as the National Endowment for the Arts, remain in business, albeit with reduced funding.

Daniel Mitchell, an economic analyst at the Heritage Foundation argues that the overall budget is what matters most to GOP reformers. "If Congress passes legislation that will balance the budget by 2002," he says, "that is a dramatic change compared with the status quo." Executives agree: Most believe any significant cuts in the deficit will help business by lowering interest rates.

**CUTTING TAXES.** A cornerstone of the GOP plan is a massive tax cut that includes family tax relief and new incentives for business. The House has passed a \$350 billion cut over seven years, while the Senate backs a \$245 billion measure that is contingent on future spending cuts. Meanwhile, Clinton wants a \$105 billion middle-class tax reduction.

Despite early predictions that the GOP would have to ditch much of its tax program because of budgetary pressure, it now appears that Congress will approve key elements of the plan. "If the Republicans get a family tax cut and a capital-gains cut, that would be Revolution with a big R," says

business consultant Kenneth M. Duberstein, former chief of staff to President Reagan.

Even though the tax cut is sure to be whittled down to \$200 billion or so, business will have good cause to crow if half of all capital gains are excluded from taxation, as proposed. And House Speaker Newt Gingrich will show that unlike Clinton, who wavered on his promise for a middle-class tax cut, the Republicans can deliver.

**MASSAGING MEDICARE.** The GOP's balanced-budget arithmetic hinges on squeezing \$270 billion over seven years from Medicare. Republicans are working on plans to restructure the program by increasing costs to seniors who seek fee-for-service care or by issuing vouchers that they can use to buy private coverage. The hope is to slow Medicare's 10% annual growth rate to 6.4%.

Democrats counter that GOP reforms would raid the Medicare trust fund to pay for a tax giveaway. Under pressure, Republicans may have to abandon structural reform and settle for traditional measures, such as lowering payments to providers.

**LIBERATING BUSINESS.** House radicals have passed sweeping reforms that would apply brakes to regulations on business and undercut enforcement of environmental, health, and safety regs. But the measures have been blocked in the Senate by moderates of both parties who view the re-

## DEREGULATION

**SUCCESS** Removing government obstacles to expansion of the fast-growing communications and financial-services industries.

**FAILURE** Special-interest lobbyists scuttle banking and often telecom reform.

**OUTLOOK** Mixed.

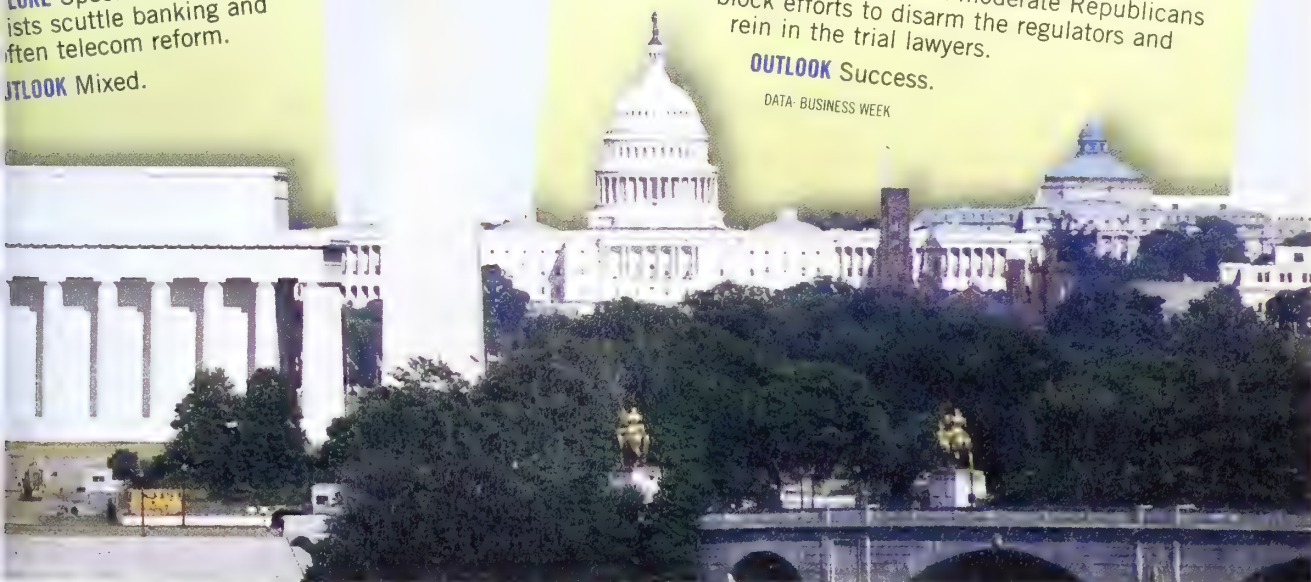
## REGULATORY RELIEF

**SUCCESS** Dramatically paring enforcement programs at EPA, OSHA, FDA, and other federal watchdog agencies. Tort reform that limits costly corporate liability suits.

**FAILURE** Democrats and moderate Republicans block efforts to disarm the regulators and rein in the trial lawyers.

**OUTLOOK** Success.

DATA: BUSINESS WEEK





forms as extreme. Although House radicals won't get all the relief they want, business is sure to be pleased that the GOP has begun to reverse years of ever-increasing federal oversight. Alexander J. Trotman, CEO of Ford Motor Co., says he's hopeful that Republicans will revamp regulations that "had little or no value to society and reduced the competitiveness of industry."

The GOP is likely to hand business a victory by passing a telecommunications overhaul that would strip controls on cable rates and relax restrictions on the number of stations a broadcaster could own. Winners are the Baby Bells, which would enter the long-distance phone business earlier than expected; some analysts think AT&T, MCI, and Sprint may fare less well with the changes.

By the time Congress wraps up work near the end of the year, one thing will be clear: The GOP will have presided over one of the most productive sessions in recent memory. To Republican commanders and their business admirers, though, the revolution has just begun.

*Susan B. Garland and Mary Beth Regan, with Paul Magnusson and Joe Carey, in Washington*

## DOLE IS HITTING CLINTON WHERE IT DOESN'T HURT

**T**he warning lights are flashing, the Presidential candidate intones grimly. American economic growth is slowing; the leading indicators are falling. Worse, wages have dropped—"the worst performance in eight years." And the incumbent President seems only too willing to tolerate slow growth, conceding, according to the challenger, that "America's economy has hit a glass ceiling."

Walter Mondale, trying to unseat Ronald Reagan in 1984? Or maybe Michael S. Dukakis in 1992, struggling to beat George Bush?

**ODD MESSAGE.** No. Those dire warnings come from Senate Majority Leader Bob Dole in the first major economic speech of his Presidential campaign. Addressing the Economic Club of Chicago on Sept. 5, front-runner Dole found himself on unfamiliar ground. A Republican traditionalist who has always backed fiscal austerity, Dole was now attacking a Democratic President for accepting subpar economic growth. It was an unlikely message coming from Dole, but one that is likely to be repeated often in the months ahead.

Dole's broadside illuminates the key strategic task facing the GOP: How can the opposition party oust an incumbent President when the economy is growing and inflation appears vanquished? Despite the second-quarter

**ELECTION '96**

pause, gross domestic product has grown at a 3.3% annual rate under Clinton—topping even President Reagan's eight-year average of 2.8%. "Dole blames Clinton for a mediocre recovery," notes former Reagan adviser William A. Niskanen Jr., "but the mediocre part was on Bush's watch." With most forecasters predicting resumed growth, Republi-



**TOUGH SELL:** Economic discontent may be rare come Election Day

cans may have a tough time finding pockets of economic discontent on Election Day.

GOP candidates hope to stir the pot by charging that Democrats are stifling growth. In a GOP Administration, Dole declares, "3% growth should be a floor, not a ceiling." The candidate promises to unleash the nation's entrepreneurs by slashing regulation, balancing the budget, and requiring that future tax increases receive a three-fifths "supermajority" in Congress. Dole also offers a vow to scrap "the whole twisted wreck of federal tax law" in favor of a flat-tax system.

Not to be outdone, Dole's competitors are also vying for the mantle of Entrepreneur-in-Chief. Senator Phil Gramm (R-Tex.) promises that he will spell out his flat-tax proposal in detail, including capital-gains and inheritance-tax relief, when he delivers his economic manifesto on Sept. 11 in Detroit. America Firster Pat Buchanan proposes stiff tariffs on Japanese and Chinese goods in order to bolster American manufacturing. And California Governor Pete Wilson says that he will cut taxes and spending so that "America's entrepreneurs will bring our nation roaring into the 21st Century."

**NO TEFLON.** But the GOP candidates are playing with fire. The "glass ceiling" that Dole decries is imposed not by Clinton econoids but by productivity growth. The U.S. can't grow much faster for long, most economists believe, without igniting inflation. One of the most influential enforcers of that view: Federal Reserve Chairman Alan Greenspan, a GOP stalwart who owes his likely reappointment next year to pressure from Dole's Senate Republicans. The only safe way to boost long-term growth is to raise workers' efficiency. But the GOP hasn't yet found the philosophers' stone to make gold out of a 20-year history of slow productivity growth.

Clinton's economic record isn't Teflon-coated. Wages have slumped in the past two years, while mergers and downsizing have undermined job security for the middle class. That could be enough to make voters receptive to GOP rhetoric. But to exploit that opening, Republican candidates will have to offer more economic details—and hope the numbers don't keep going against them.

*By Mike McNamee in Washington*





**WHERE DID THEY GO?** *This year, fewer foreign tourists*

## THE ECONOMY

# SUDDENLY, SERVICES AREN'T SUCH WORLD-BEATERS

Exports are stalled—bad news for the overall trade deficit

The Japanese have their electronics, the Germans their engineering. But when it comes to command of global markets, the U.S. owns the service sector. It's the world leader in exporting everything from data security to crowd control. Such global supremacy allowed exports of U.S. services to grow at a double-digit annual clip as recently as '91—one of the few bright spots in the U.S. trade picture.

The party seems to be winding down, though. For the first half of 1995, as U.S. exports in manufactured and farm goods jumped 16.3%, service exports climbed a measly 5.4% (chart). Service exports have actually stalled since last September, at around \$17 billion per month. That's putting the brakes on what was a key growth engine for U.S. trade.

**POLITICAL FALLOUT.** These numbers have potentially explosive political ramifications. The annual surplus in service—expected to hit \$60 billion this year—typically offsets a third of America's huge and growing deficit in goods trade. With service exports stagnating, the overall U.S. trade deficit in goods is projected to balloon to a record \$188 billion this year. And the widening trade gap could well

give new ammunition to economic nationalists such as GOP Presidential contender Patrick J. Buchanan, who opposes Bill Clinton's drive to lower trade barriers worldwide.

Politics aside, however, just how significant are the new numbers? Oddly enough, the way government bean counters tally the totals, an important factor in the slowdown could be only temporary. Tourism accounts for about 30% of the U.S.'s service exports: Every hotel stay by a foreign traveler to the U.S. adds to the total. Even with the dollar at historically low levels, the Travel Industry Assn. expects a 4% drop in tourism to the U.S. this year, led by a falloff of 9% of visitors from Canada and a 15% drop in Mexican visitors. Those numbers, of course, are likely to im-

prove as the Canadian and Mexican economies rebound.

More troubling is weakness in another category of service exports, which includes consulting, advertising, and engineering services performed from a U.S. office for an overseas client. In the first six months of this year, growth in that sector, which also accounts for about 30% of total services exports, was running at just 4.4%, down from 8.1% in the first half of last year.

However, puzzling out the reasons for the drop-off is tough because the category is a catch-all of business services. Many companies are doing well: Hollywood is having a

banner year abroad, for instance. But sluggish overseas economies are taking a toll on others. For example, a survey by *Engineering News Record* found that foreign billings for U.S. engineering companies fell to \$3.5 billion in 1994, 31% less than the previous year. The main reason: a plunge in commissions from the Middle East. Foreign purchases of U.S. equities were off earlier this year, too.

More generally, after years of explosive growth, many economists argue that the slowdown is inevitable. "Service exports shot up from a low base in past years, and growth has been phenomenal," notes Lehman Brothers Inc. economist Allen Sinai.

In purely economic terms, though, the effects of the service slump may be far less worrisome than politicians would have people believe. Under the government's definitions, all sorts of activities abroad—from McDonald's hamburger sales in Moscow to ads created abroad for a foreign client—don't count in the trade report. Many economists think the government simply misses many key foreign billings by U.S. companies because the numbers are so hard to track. "Everyone knows that service exports are mismeasured and often not tallied,"

says J. David Richardson, a visiting fellow at the Institute for International Economics in Washington.

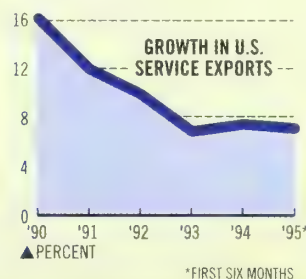
Still, the trend in the numbers is clear, and troubling if it lasts. Clintonites still dream of filling the trade gap with an ever-growing services surplus. They may be in for a rude awakening.

*By Amy Borrus in Washington, with Ronald Grover in Los Angeles*

### GOT THE GOODS...



### ...BUT NOT THE SERVICES





## COMMENTARY

By Seymour Zucker

# CUTTING THE DEFICIT WON'T BEEF UP THE DOLLAR

**N**ursing a broken thumb, Fed Chairman Alan Greenspan told the assemblage of economists and monetary experts in Jackson Hole, Wyo., on Sept. 1 that it may have been the "consequence of excessive fine-tuning." Indeed, Greenspan got high marks for his monetary twiddling, which has slowed the economy without pitching it off a cliff.

But some top-gun economists at the Federal Reserve Bank of Kansas City annual conference were thumbs-down on Greenspan when it came to the dollar. They challenged his view that cutting the budget deficit could boost the value of the greenback. Laurence Ball of Johns Hopkins University and N. Gregory Mankiw of Harvard University sparked the attack, dubbing as "fallacious" Greenspan's contention that the high deficit is to blame for the weak dollar—and that balancing the budget would send it climbing. Just the opposite is true, they maintain: A lower deficit leads to a lower dollar, and a higher deficit pushes the dollar higher. **RATE BAIT.** The Ball-Mankiw argument is strong. Here's the logic behind it: A growing deficit means the government must borrow more, pushing up interest rates. As U.S. interest rates rise relative to the rest of the world's, money flows out of foreign assets and into U.S. securities. This capital flow raises the dollar's value because to buy U.S. securities, foreigners must dump their own currencies and buy dollars.

Conversely, a decreasing deficit lowers government borrowing and thus pushes interest rates down. As rates fall, investors seek higher returns overseas. They sell dollars and buy foreign bonds. The result: a depreciating dollar. "No question about



it," agrees Harvard's Martin Feldstein. "Cutting the deficit means a lower dollar."

Greenspan concedes that the Ball-Mankiw makes sense in theory, but he contends that in practice it would be offset by another factor: A cut in the deficit would reduce inflationary expectations, making U.S. assets less risky and more attractive to investors. Foreigners, rather than selling dollars, would be buying them. So the dollar would rise, not fall like the economists were arguing.

Greenspan's case is the weaker one. For one thing, inflationary expectations are largely based on monetary policy. If the Fed is holding a tight grip on the money spigot, inflationary expectations will be dampened—even if the federal deficit rises. Look at Japan: Its deficit has rocketed to a projected 4.1% of gross domestic product this year—more than three times what it was two years ago. That hasn't heightened

the risk of holding Japanese bonds, though, because the Japanese have kept money tight. And what of the yen? Even as Japan's deficit has ballooned, it has remained rock-solid.

**MYTHICAL POWER.** The U.S. experience seems less clear, but it, too, calls into question the Greenspan line of reasoning. During the mid-1980s, as deficits exploded, the dollar soared. And over the past year and a half, the commitment in Congress to balance the budget has intensified, yet the dollar has weakened. Robert Johnson, an economist and trader at Moore Capital Markets, put it this way: "If I'm sure the deficit is coming down, then I short the dollar." Even within the Fed research staff, there is some dispute over whether the boss is right.

If budget-cutting were to lift the dollar, as Greenspan suggests, fiscal discipline would have a devastating effect. Not only would the economy slow because of the cut in government spending, but the higher dollar would cause exports to fall, while imports would take off.

Somehow, a strong dollar makes people feel that all is well with America. So it may be almost natural to associate a robust dollar with a government that is finally balancing its budget. However, it was a strong dollar in the 1980s that almost decimated U.S. industry, pricing its products out of world markets. And it has been the declining dollar that has helped make America competitive again. Thumbs up, then, for budget-cutting and what is likely to follow: a lower dollar.

*Senior Editor Zucker directs BUSINESS WEEK's economics and markets coverage.*

Greenspan's theory that red ink weakens currencies is undercut by the yen now and the dollar in the mid-'80s





## MARKETING

# WHY CLOTHIERS ARE FEELING PINCHED

Shoppers are waiting for markdowns and driving hard bargains

Corporate lawyer Marsha Kolb spent the beginning of Labor Day weekend shopping for her fall wardrobe. The 32-year-old Mundelein (Ill.) resident found a \$320 black-and-white-pin-striped pantsuit that would be perfect for work. But Kolb didn't buy it: She'll wait back in October, when the weather is cooler and the prices are lower. "I know the price will come down at least a third during the next sale," she says. "I'm not going to pay full retail. That would be ludicrous."

Kolb is hardly alone. Personal incomes are up, and the recession is long past, but apparel sales have been dismal since 1991. Instead of getting a boost from back-to-school buying in August, merchandisers found themselves stuck with racks of fall clothes during a swelling summer. Chains such as Federated Department Stores Inc. and May Department Stores Co. posted measly same-store sales increases of less than 1% during the month, while retailers like Ann Taylor Inc. and The Limited Inc. posted declines of 11% and 12% respectively.

**DEADEN BOOM.** Even optimistic retail executives are wondering how often they can blame the weather for the lingering malaise. Last year, they cursed the mild winter. Next, they complained about the exceptionally chilly spring. Now, it's the heat. When the weather's not to blame, it's the lack of a strong

fashion trend or a shift in spending priorities of baby boomers.

Boomers, though, have never gone in much for self-deprivation: Their closets, in fact, are bulging with recent purchases, says David Poneman, senior retailing analyst at Sanford C. Bernstein & Co. in New York. Deflation in clothing price tags has masked a hidden boom in unit sales, he argues. Over the past three years, clothes prices have fallen by almost 10%, compared with the economy's overall price level, putting them lower than they were four years ago.

Shoppers such as Kolb are still buying, but they're waiting until the stuff is marked down. "It's chic to be cheap," says Robert Buchanan, retail analyst at NatWest Securities Inc. "Folks delight in going shopping and not spending much money."

Apparel sales in the first half of 1995 totaled \$60 billion, an increase of 2% from the 1994 period. But unit sales were up almost 5% during the same period, to 6.9 billion, according to NPD Group, a Port Washington (N.Y.) research firm that tracks retail data. Meanwhile, the share

**BULGING RACKS:** Too many shops mean falling apparel prices

of women's wear bought on sale rose slightly in the first six months of 1995, to 51.5%. "So much stuff has been sold on sale, consumers have been conditioned to wait," says Michael Hand, NPD vice-president for soft-goods services.

What's behind the weakening prices? There are just too many stores chasing too few apparel dollars, says NatWest's Buchanan. And market conditions are unlikely to improve anytime soon, as giant retailers and discount chains such as Sears and Target Stores expand their apparel offerings.

**PHONE ALERTS.** Retailers are trying to adjust. Hoping to lure preseason shoppers, Marshall Field & Co., a unit of Dayton Hudson Corp., sent out coupons good for \$75 off August purchases of \$300 or more for fall designer clothes. Others, such as Gap, The Limited, and Ann Taylor, which control the manufacturing of their private-label clothes, are trying to roll out new fashions closer to the actual wearing season, say retail consultants. But given August's disappointing sales, there's little evidence the strategy is working.

Rather than fighting the trend, a growing number of upscale retailers, such as Nordstrom, Saks Fifth Avenue and Neiman-Marcus, are going with the flow. Instead of pushing for a full-price purchase, sales assistants are offering to telephone their customers when specific items go on sale. Anne Trudel, a Potomac (Md.) real estate agent, figures that she has managed to cut clothing bills by 25% to 40% this way. "They really want to move the merchandise, and they've figured out this is what it takes," she says.

Still, many merchandisers remain optimistic the malaise will go away soon. When retail consultant Kurt Salmon Associates surveyed 45 retailers about 1996 sales expectations, 84% said they anticipated dollar sales to increase next year, with close to half expecting sales to rise more than 5%. But

they had better not be counting on shoppers like Marsha Kolb with her bulging closet. Clearly, it's going to take more than a change in the weather to give apparel sales a good kick in the pants.

By Susan Chandler in Chicago, with Ann Therese Palmer in Lake Forest, Ill.





## MARKETING

### IT'S ENOUGH TO MAKE YOU SICK

Nearly identical drugs are sold as if they had major differences

In days long past, relief of acid indigestion was a relatively simple matter. We ladled on the chili, dug into pepperoni pizza, and topped it off with Aunt Leona's killer brownies, secure in the knowledge that our Tums or Alka-Seltzer were waiting patiently in the medicine cabinet. Oh, what a relief it was.

Now, drug goliaths are pelting consumers with a slew of reformulated big-time prescription remedies. Pepcid AC and Tagamet HB have arrived. Zantac is coming. And the ad climate is getting ugly. "If the public could actually see and make sense of the data on which these claims are based, they would be appalled at how trivial the differences are," says Dr. Jerome L. Avorn, an associate professor at Harvard Medical School. "It's all puffery."

Or worse. On Sept. 5, Johnson & Johnson-Merck, the joint venture that produces Pepcid AC, sued SmithKline Beecham, maker of Tagamet HB. J&J-Merck alleges false advertising, citing SmithKline's claims that Tagamet HB works much faster. SmithKline had sued J&J-Merck on Aug. 25, citing boasts so bald as "New Pepcid AC is better than Tagamet HB."

**VIRTUAL TWINS.** Certainly, the pharmaceutical world has seen this sort of fracas before. With the introduction of two major acid indigestion products and more on the way, though, the OTC wars have reached a new frenzy. Drugmakers are spending more than \$250 million to sell their wares to the 61 million Americans with occasional heartburn, a market worth well over \$1 billion a year. All that money, say critics, forces queasy consumers to sort through irrelevant or misleading ads. J&J-Merck's ads claim

"Only Pepcid AC has proven that it can prevent heartburn and acid indigestion." SmithKline trades on Tagamet's history as a prescription ulcer-fighter—a far cry from its weaker over-the-counter version.

Many doctors contend that, ultimately, the OTC forms of Pepcid and Tagamet simply are not much different. Both so-called

### TWEEDLEDUM AND TWEEDLEDEE?

*Competing claims in ads for Pepcid AC and Tagamet HB and a doctor's reaction:*

**PEPCID AC** "Only Pepcid AC has proven that it can prevent heartburn and acid indigestion. Only Pepcid AC controls acid with just one tablet. Only Pepcid AC is preferred by 8 out of 10 doctors and pharmacists."

**TAGAMET HB** "Doctors have already endorsed Tagamet in the strongest possible way. With their prescription pads. And now doctors and pharmacists will appreciate Tagamet HB's onset-of-action for heartburn. Pepcid AC, on the other hand, can take one to two hours to start reducing stomach acid."

**M. MICHAEL WOLFE, HARVARD MEDICAL SCHOOL** "These drugs are virtually the same." And neither acts as quickly as such antacids as Tums or Mylanta.

H2-antagonists inhibit the production of stomach acid, not just absorb it, as antacids do. "These drugs are virtually the same," says Dr. M. Michael Wolfe, an associate professor of medicine at Harvard and co-author of *The Fire Inside*, a gastrointestinal guide due out in February. "The differences are not clinically relevant."

For marketers, though, it's crucial to fix the idea of product superiority early on—as SmithKline learned when rival Glaxo Inc. convinced doctors in the mid-1980s that its prescription ulcer-fighter Zantac outperformed Tagamet. Although almost identical, Zantac soared above Tagamet to become the biggest-selling drug in the world, racking up \$3 billion in annual sales. Indeed, the ad battle

among H2-blockers will heat up when Glaxo and marketing partner Warner Lambert Co. take Zantac over the counter, perhaps later this year.

Already, the battle is forcing marketers to do some fancy dancing. J&J-Merck must pitch its Pepcid without killing off its Mylanta antacid. So, while vaunting Pepcid AC's advantages in one set of ads, J&J-Merck claims in others that "nothing soothes heartburn faster than Mylanta liquid." SmithKline, for its part, shuns attacks on antacids such as its Tums in promoting Tagamet HB. That's likely a sound strategy, since it and the other combatants probably will end up marketing their H2-blockers in combination.



with an antacid. More to the point, doctors say that Tums, Mylanta, and Maalox provide almost immediate relief, even if slower-acting H2-blockers ease discomfort longer.

What doctors think, though, may matter on Madison Avenue. "If you're targeting doctors or the medical community, the advertising may frankly not be credible," says Gary M. Stibel, principal at the New England Consulting Group. But he adds: "Doctors are very naive in believing that small differences between products cannot be meaningful to consumers." In the end, he says, what matters is "what real consumers believe is important." Look for more advertising heartburn to come.

*By Joseph Weber in Philadelphia*

A tall, olive-green metal radio unit, identified by a label as a U.S. Army Signal Corps Radio Receiver and Transmitter BC-611. The unit features a large speaker on the left side, a microphone on the right, and a label with technical specifications. The label includes the text: "SIGNAL CORPS", "U.S. ARMY", "RADIO RECEIVER AND TRANSMITTER BC-611", "10031 PRIME 4301", "GALVIN", "10031 PRIME 4301", and "10031 PRIME 4301". The unit is shown in a close-up, vertical view.

A black mobile phone with a large antenna and a numeric keypad, shown next to a small electronic component. The phone is a classic candy-bar style with a large antenna on top. The keypad is numeric with some function keys. The screen displays "581212". The small electronic component is a black rectangular board with various components and a connector.





## PEOPLE

### KERKORIAN KEEPS 'EM GUESSING

What's behind his hiring of Chrysler veteran Jerry York?

**A**t Chrysler Corp., the omnipresent question is this: What will Kirk Kerkorian do next? For five months, the Las Vegas gambling mogul has hovered with his 13.6% stake in the car-maker. Even after abandoning his underfinanced \$20.5 billion acquisition bid in May, his presence continues to rattle managers and investors.

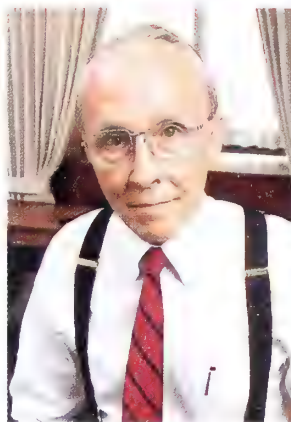
On Sept. 5, Kerkorian played his latest card: hiring Jerome B. York, chief financial officer at IBM and a 14-year Chrysler veteran. York becomes vice-chairman of Tracinda Corp., Kerkorian's investment vehicle. More important, he may be Kerkorian's choice to run Chrysler, if the moribund takeover bid is resuscitated. One Kerkorian intimate says that the billionaire investor is still contemplating a proxy solicitation to attempt to gain control of Chrysler's board or to force dividend increases or stock buybacks.

York, 57, gives Kerkorian a formid-

able boost. A proven cost cutter and crisis manager, he was a key architect of IBM's \$8 billion cost-cutting plan and a leader of Chrysler's early-'90s crusade to chop \$4 billion in operating costs. During his years at Chrysler, he ran the company's Mexican operations, was general manager of the Dodge division, and was briefly one of the company's top engineers. "He does add some credibility" to Kerkorian's demands on the company, concedes one Chrysler executive.

**LONG ODDS.** That may be crucial, since York's former boss, Lee A. Iacocca, could soon sever his ties with Kerkorian. Iacocca has supported Tracinda's bid from the beginning. But now, he is negotiating with Chrysler directors to regain access to stock options that are worth approximately \$40 million. In return for freeing the options, directors are demanding Iacocca cut his alliance with Kerkorian. Directors could vote on Iacocca's request as early as Sept. 7.

Even with York, however, the odds of Kerkorian's taking control of Chrysler remain long. Financing for the buyout,



**PROVEN RECORD:** York may boost Kirk's credibility

now valued at roughly \$1 billion, is still in question. And even though a proxy fight might put York on Chrysler's board, electing an entire York-led majority slate of new directors would be much more difficult. Analysts, meanwhile, expect strong sales for Chrysler's new minivans to kick-start profits over the next year. Investors "would have to think twice about throwing out current management, given what they have done," says Robert Miller, former Chrysler vice-chairman and now of

of Morrison Knudsen Corp.

York, who declined to discuss his new job, will be well paid in any case: He is to receive a percentage of the gain from Tracinda's Chrysler shares, an arrangement already worth \$20 million. Generous, yes—but Kerkorian certainly can afford it. He added a cool \$130 million to his own paper profit when Chrysler's stock jumped by \$2.50 a share, to 57, the day of York's hiring. That's enough to hire several Jerry Yorks—and still have some cash left over.

*By David Woodruff in Detroit, and Ira Sager in New York*

## STRATEGIES

### A BIG LITTLE BANK DEAL

NationsBank won't make history with it—just money

**C**redit the rumor mill with this much: Acquisitive Chairman Hugh L. McColl was indeed working on a takeover. But it wasn't Bank of Boston, First Chicago, or Chase Manhattan—all reported NationsBank Corp. targets in recent weeks. Nothing, even, that would broaden the nation's third-largest bank's reach outside its stronghold in the Southeast.

Instead, NationsBank is acquiring small-fry Bank South Corp. for the almost quaint price of \$1.6 billion in stock. You could all but hear Wall Street deflate with disappointment. "Can you believe that a \$1.6 billion deal is trivial?" asks NationsBank President Kenneth D. Lewis. "It's a sign of the times."

The deal doesn't accomplish what

many expected of McColl: A landmark acquisition with the scope of Chemical Banking Corp.'s \$10 billion purchase of Chase. But trivial it's not. The purchase consolidates NationsBank's position in the hot Atlanta market, blocking Wachovia Corp. or SunTrust Banks Inc. from nabbing Bank South. "This is a signal to the nation that the show isn't over in the South," says Interstate/Johnson Lane Inc. analyst John J. Mason.

At a hefty 2.5 times Bank South's book value, NationsBank is spending big by McColl's standards. But it will pay for the purchase with its own inflated stock, up 40% on the year. And the in-market combination allows

for far more consolidation than buying the Northeast would: NationsBank plans to eliminate 100 of the combined bank's 337 Georgia branches. That should trim \$174 million in operating costs, it says, and make the acquisition a contributor to earnings by 1997.

The deal underscores NationsBank's plan to emphasize retail banking, even as it builds its "wholesale" presence in loan syndication and capital markets, a fit with McColl's strategy of growth through acquisitions in the South. All the big one? Investment banking sources say McColl has considered bids for Bank of Boston and Chase—then backed off when the prices got too high. Lewis believes the Bank South acquisition strengthens NationsBank's home front and enables McColl to "wait for another deal that makes sense." The question: With banks succumbing most weekly, how long can McColl afford to wait?

*By David Greist in Atlanta*

NUMBER OF BRANCHES  
■ NATIONS BANK  
■ BANK SOUTH



### SMART MOVE

The deal allows more consolidation than buying in the Northeast would: NationsBank plans to close 100 branches





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## EXECUTIVE SUITE

# DIVORCE, EXECUTIVE STYLE

A soapy drama envelops two former Thrifty PayLess officials

**N**o matter who you believe, it has been a pretty messy divorce. The estranged husband claims his wife was stolen by her onetime boss, the former chief executive of Thrifty PayLess Inc., the nation's second-largest retail drugstore chain. The wife says that's bunk and claims her soon-to-be-ex is trying to punish her for leaving him.

The nasty affair surfaced when the husband, David Nelson, 36, filed a lawsuit on Aug. 15 alleging that former Thrifty PayLess CEO Timothy R. McAlear hired Nelson's wife as marketing vice-president at nearly six times her previous salary to continue a "secret romantic and sexual relationship" with her. Nelson is suing McAlear and Thrifty PayLess for allegedly inducing him to leave a better-paying job and follow his wife to Oregon.

**NO PAIN.** Both McAlear, 51, and Lori Young Nelson, 32, were ousted from their jobs by Thrifty PayLess last December. The company won't comment, but it doesn't appear that Thrifty PayLess' financial performance was wanting while they were there. McAlear led PayLess

Drug Stores Northwest Inc. through its December, 1993, merger with Thrifty Corp. after PayLess was spun off by Kmart Corp. On the day the board announced his departure, the company reported earnings before accounting changes of \$106 million on sales of \$3.1 billion for the year ended Oct. 2.

That apparently was enough to qualify McAlear for a \$248,772 bonus tied to profits: McAlear has sued PayLess for the bonus and damages for what he says was an unfair dismissal. Lori Nelson is also suing the company for a bonus of about \$55,000 she says is due her.

Both McAlear and Lori Nelson filed for divorce from their spouses last

March. But they vigorously deny that David Nelson has any grounds for a suit. "The whole thing is a fairy tale," insists McAlear. "They say there is nothing more dangerous than a woman scorned, but I guess a man's scorn can be worse."

Lori Nelson says her husband simply resented her quick rise: "When I decided to divorce him, David said: 'I will make your life a living hell.'" David

offered the job of marketing vice-president at PayLess. "She was a star, rising very fast," says Samuel H. Pettway, SpencerStuart headhunter.

From there on, the story gets murkier. David Nelson alleges that McAlear arranged for Lori to receive a compensation package of more than \$300,000 a year, almost six times her income at Walter Thompson. McAlear says it was "about half that amount" and contends the package was standard for an executive of Lori Nelson's caliber.

Nelson, then making \$70,000 in salary and commissions as a territory manager for Club Car, says he was flown first class to Oregon to meet with McAlear. Over lunch and dinner, McAlear told him his wife would receive stock worth up to \$4 million, Nelson alleges in the suit he filed in Oakland County Circuit

Court in Michigan. Given the benefits to his wife, Nelson decided to transfer to a less-lucrative sales region in Oregon, he says, where his income fell to \$40,000 last year.

Meantime, Kmart sold PayLess to Thrifty within months after Lori Nelson joined the company. McAlear, who began as management trainee with Kmart in 1963, emerged as CEO of the newly combined company, which projects sales of \$4.6 billion this year from its 1,100 drugstores. And in April, 1994, Lori Nelson was promoted to senior vice-president.

What David Nelson didn't know when Lori was first offered the job, he says in the suit, was that by Aug. 1, 1992, his

wife was having an affair with McAlear, then married to his second wife. He says he only discovered the affair in March, after Lori filed for divorce.

Lori Nelson tells a different story. She says her marriage had long been troubled. "[David] is insecure and paranoid," she contends. "He has accused me of being involved with every superior I ever had." They had been separated for a year before he decided to move to Oregon with her. Once there, she charges, David "sat around and didn't go to work."

The only thing missing, it seems, is Hollywood. Mercifully, the parties involved all say they have yet to be contacted about a movie deal.

*By John A. Byrne in New York*

## A TALE WORTHY OF MELROSE PLACE

**JUNE 1993** Lori Young Nelson joins Thrifty PayLess as vice-president for marketing

**DECEMBER 1994** Thrifty PayLess ousts both CEO Timothy McAlear and Nelson

**MARCH 1995** Both McAlear and Nelson file for divorce from their spouses

**AUGUST 1995** Nelson's husband sues McAlear, alleging the CEO had a "secret and sexual relationship" with Nelson's wife

DATA, COURT DOCUMENTS, OAKLAND COUNTY, MICH.



Nelson declined to be interviewed, but his attorney, Gerard Mantese of Huntington Woods, Mich., says he is confident of winning the suit. "My client is on the side of the angels," says Mantese.

This story began at Northern Michigan University, where the Nelsons, business students, met. They married in 1989 and David got a job selling golf carts for Club Car Inc. Lori joined ad agency J. Walter Thompson USA Inc.'s Detroit office as an account executive.

In 1991, she was assigned to the advertising account of PayLess, where she began to work closely with McAlear, then president and based in Oregon. Lori soon was promoted to vice-president at Thompson and in mid-1993 was





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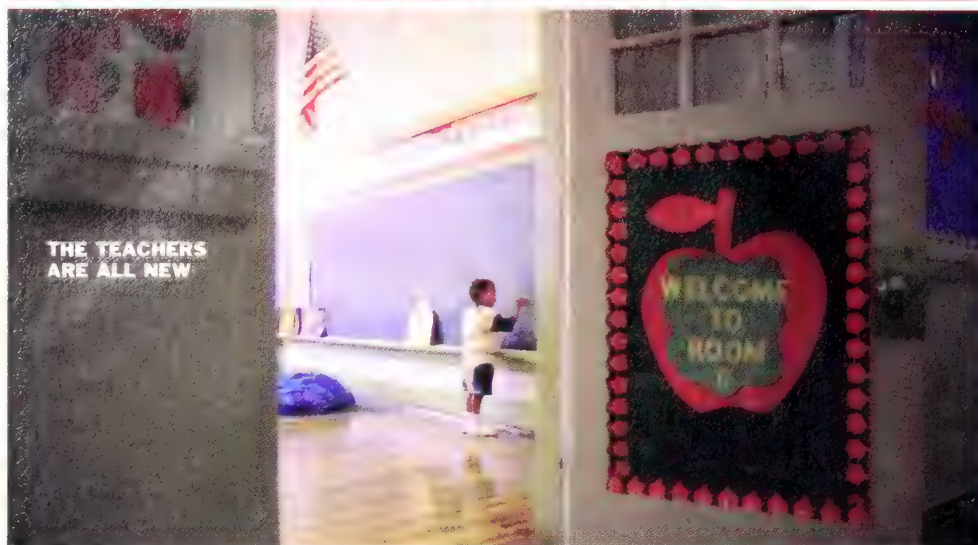
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## ALTERNATIVE'S ALTERNATIVE

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**PEG** teachers' pay to performance

**DESIGN** its own curriculum; offer special programs before and after school

## EDUCATION

# READING, WRITING, AND RANCOR

A bitter fight looms over privatization of a Pennsylvania school

**B**everly Hillman can't pin down exactly when or why Turner Elementary School hit the skids. In the '70s, she says, her daughter got a good education at the highly ranked school in the Pittsburgh suburb of Wilkinsburg. But as the local steel industry died and Wilkinsburg grew poorer, Hillman has been frustrated by the school's deterioration. The last straw came when two boys beat up her 8-year-old granddaughter in an empty hallway. "They just let those kids sit there and ferment," complains Hillman.

Now, however, Hillman is convinced that Turner is in for a turnaround. Last spring, the Wilkinsburg school board hired a fledgling private company, Alternative Public Schools Inc., of Nashville, to run it. APS, co-founded in 1992 by financial consultant John Eason, has tapped leading educators to devise a new program for Turner. Its approach is largely based on a program developed by Elaine Mosley, former principal of an innovative inner-city school in Chicago who now is taking over as principal of Turner. The project—the APS's first—stresses a longer school year and study programs tailored to each of Turner's 400 students. APS also fired Turner's 24 teachers and hired, at comparable pay, its own 26-member staff.

The changes at Turner Elementary have implications for education that go

far beyond the town of Wilkinsburg. Indeed, cities and states across the country are fiercely debating the role of teachers' unions and private companies in public schools. Other school districts in cities such as Baltimore and Hartford have also hired private companies to administer existing school systems. But Wilkinsburg is the first district to give over an entire school's curriculum and staff to a private company.

**POWERFUL PALS.** The local union, the Wilkinsburg Education Assn., views Turner's privatization as a mortal threat and is suing to kill the initiative. The case is scheduled to come before the Pennsylvania Supreme Court on Sept. 18. "They want to bust the union," says Pennsylvania Education Assn. Field Director Edward W. Christy, "and they're hiding behind the issue of improving the schools." Even if the union loses its court battle, it hopes to win control of the school board in elections this fall and then rescind the contract.

But the Wilkinsburg school board has powerful supporters. One is Pennsylvania Governor Tom Ridge, who's pushing hard for a school-voucher system in the state. And the conservative Landmark Legal Foundation of Kansas City, Mo., is paying all the board's legal bills. The teachers are backed by the state chapter of the National Education Assn., the nation's largest labor

union, which is also funding the campaign to unseat the school board and subsidizing grassroots opposition to the Turner plan.

As the politics rage, APS is scrambling to win community support. Without increasing Turner's \$2 million budget, the company is extending the school year to 11 months and lengthening the day: Kids can stay at Turner from breakfast at 7 a.m. through special activities ending at 6 p.m. That means more contact with teachers and fewer idle hours on the mean streets of Wilkinsburg. In addition to long hours, the new teachers are expected to knock on doors throughout the district, establishing ties with parents and—equally important—winning political support for the Turner initiative.

Sounds like a tough job? That's the idea, says APS President Eason. He maintains that if teachers know their jobs hinge on parents' satisfaction, they'll work longer and harder. In time, he expects many private companies, including APS, to bid for school contracts throughout the country, generating a market-driven revolution in education.

But the teachers' union charges that the Wilkinsburg board is blaming deep social problems, from poverty to white flight, on teachers. What's more, privatization opponents claim that by firing the 24 teachers at Turner and replacing them with younger ones, mostly from outside the borough, the board is severing Turner's roots in the community.

Even if the experiment at Turner survives court and local challenges, the new teachers face a series of daunting hurdles, from lifting test scores to improving discipline. Otherwise Turner private educators will be facing both angry parents and angry employers.

By Stephen Baker in Wilkinsburg, Pa.



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 **TEXAS  
INSTRUMENTS**



EDITED BY KEITH H. HAMMONDS

## KODAK TAPS TWO YOUNG TURKS

FOR HIS FIRST 21 MONTHS AT the helm of Eastman Kodak, George Fisher surprised nearly everyone by leaving in place most of Kodak's old management team. But on Sept. 5, he decisively reshuffled the top ranks, promoting two younger executives to work directly under him as assistant chief operating officers—and announcing the retirement next May of the company's current No. 2 manager, Leo "Jack" Thomas. Insiders say that the two rising stars, Carl Kohrt, 51, and Daniel Carp, 47, are in the Fisher mold: incisive, personable, and candid. The promotions have set in motion an early race to succeed Fisher,

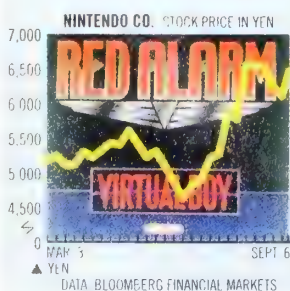
although at 54 he's not likely to retire anytime soon.

## COMMERCE SPINS OFF THREE INDEXES

PRIVATIZATION MARCHES ON: On Dec. 29, the government's primary gauge of future economic conditions moves to the private sector. The index of leading indicators will be computed and published by the Conference Board, a New York-based business research group known for its surveys of consumer confidence. The Commerce Dept. is spinning off the 47-year-old index—along with its siblings, the lagging and coincident indicators—to save about \$450,000 a year, funds that will be devoted to improving other statistics. The three indexes are second-hand figures derived from other government and private statistics, but they can still move markets: "A proven record in data security" was one of the Conference Board's prime qualifications.

## ANOTHER WIN-WIN95 PROPOSITION

HOW TO MAKE A BUNDLE in software—lesson two. Having sold one million copies of Windows 95 in just four days, Microsoft now estimates that more than 10% of Win95 buyers also have purchased its new Office for Windows 95, a collection of spreadsheet, word processing, and other programs. For that, it can thank the noncompetition. Lotus Development—now owned by IBM—on Sept. 5 announced a Win95 version of its SmartSuite offering. But critical elements, most notably the 1-2-3 spreadsheet, won't immediately take advantage of Win95's many features. Also, Novell won't offer a Win95 version of its PerfectOffice until at least yearend.



## HEADLINER: JERRY JONES

### A COWBOY THE NFL CAN'T LASSO

When Jerry Jones paid \$140 million for the Dallas Cowboys in 1989, it was no ego play. He intended to make money. So he has.

On Sept. 4, the defiant one struck again at the National Football League establishment, announcing a seven-year agreement between his Texas Stadium and Nike. Nike will supply sideline togs to Cowboy players and coaches and there will be a joint development of a football theme park.

NFL Commis-

sioner Paul Tagliabue says the deal violates league policies. Tough. Such deals will allow Jones to pay bonuses that bypass the NFL's salary cap. Big bonuses win big players, who win big games—which make money.

Jones may have more in store: Sports Marketing Group chairman Nye Lavalley says a pact with American Express is imminent. The NFL's official charge card is Visa.

By Stephanie Anderson Forest



## USAIR'S CHIEF PLANS TO BAIL OUT

ON SEPT. 5, USAIR PREDICTED it would end 1995 with an operating profit, its first in six years. The next day, Chief Executive Seth Schofield, 56, abruptly announced his intention to retire. The reason wasn't clear. Schofield "had decided that USAir had come a long way," a company spokesman says. Indeed, since taking over the airline in 1992, he has fought with unions to cut salaries and other operating expenses. But the airline still has the industry's highest labor costs, and its stock hasn't budged.

## LABOR LOBS ONE AT FIELDCREST CANNON

IN A BATTLE AS BITTER AS any in the textile industry's long, troubled labor history, the Union of Needletrades, Industrial & Textile Employees

has won a big round. The National Labor Relations Board ruled over the Labor Day weekend that Fieldcrest Cannon must allow employees to hold new union elections, reinstate 14 union supporters fired during a 1991 union election and repay \$2 million in back wages. The real capper: Fieldcrest Cannon vice-president must stand by while a NLRB cease-and-desist order read aloud at Fieldcrest plant in four states. Fieldcrest Cannon plans to appeal.

## ET CETERA...

- Swiss Bank will acquire 24.9% stake in Perot Systems, for an undisclosed sum
- Time Warner Cable will swap its Savannah, Ga. system with Jones Interchange
- PP&L Resources rejects Peco Energy's \$3.8 billion takeover proposal
- U S West couldn't agree on terms of its \$800 million investment in Cablevision.



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## AND THE HOT-BUTTON ISSUE FOR '96 IS ... FREE TRADE?

That dull boom you hear in the distance is the opening salvo of the '96 Presidential campaign. Bill Clinton is blasting away on the "Three Es," hitting Republicans for gutting education, the environment, and elders' Medicare benefits. The GOP is firing back at Clinton for being soft on criminals, welfare chiselers, and illegal immigrants. Yet despite the partisan bombast, both sides are ducking an explosive issue that's starting to stir voters: surging economic nationalism.

For now, the charge that free-trade policies are costing the U.S. jobs is coming from the periphery: America Firster Patrick J. Buchanan, civil rights leader Jesse Jackson, and independent Ross Perot. But with the North American Free Trade Agreement and a new global trade pact yet to produce the promised economic payoff, protectionism may go mainstream. "It could be the hot-button issue for '96," says Democratic pollster Rob Schroth. "It touches on all the things that concern people: their wallets, immigration, foreign aid."

The protectionist backlash has already prompted Clinton to put the brakes on trade expansion. Fearful of riling economic nationalists in both parties, the President won't fight for renewed authority from Congress to negotiate trade deals on a "fast track." Without that power, he has no chance of extending NAFTA to the rest of Latin America.

**BUCHANAN FODDER.** The GOP front-runner, Senate Majority Leader Bob Dole (R-Kan.), is also trimming his sails. Dole took a pummeling at Perot's mid-August issues confab when necklers cried: "What about NAFTA?" Since that public thrashing, the veteran free-trader has clammed up on the subject.

Indeed, NAFTA has become the rallying symbol of the nationalists, who blame it for turning a \$1.3 billion U.S. trade surplus with Mexico into a \$12 billion deficit while boosting illegal immigration. In fact, the accord has cushioned the impact of

Mexico's financial crisis on American exports by preventing Mexico from hiking tariffs on U.S. goods. But facts aren't the issue here. Instead, NAFTA-bashers have made emotional inroads in convincing the public that the pact was a deal with El Diablo. A new national survey by EPIC-MRA, a nonpartisan Lansing (Mich.) polling firm, found only 41% support for a free-trade deal with Europe, despite traditionally warm U.S.-European ties. Activist Ralph Nader hopes to fuel opposition with a study, released on Labor Day, that ridicules unfulfilled corporate pledges to boost U.S. jobs under NAFTA.

The protectionists' alarms tap into deep fears among U.S. workers that free-trade policies are exporting American jobs to low-wage nations. Buchanan, currently second in New Hampshire polls, says his populist campaign is "touching a nerve with people who want leaders to start looking out for American workers first." His solution: abrogation of NAFTA, withdrawal from the World Trade Organization, and punitive tariffs on imports from Japan and developing nations.

**WORKER FURY.** Proposals like that have U.S. exporters jittery. "The U.S. market is simply not big enough" to sustain economic growth without exports, says Tracy J. O'Rourke, CEO of Varian Associates Inc. and chairman of the National Association of Manufacturers.

True enough. But rational arguments may be no match for the fury workers feel after years of layoffs and stagnant wages. Says Senator Richard G. Lugar (R-Ind.), a dogged free-trader: "People are searching for a scapegoat."

That's why naysayers are in the ascendancy. In the long run, globalization may prove as inexorable as the Industrial Revolution. But given today's widespread economic insecurity and the brutal Presidential campaign ahead, some short-term trade retrenchment may be inevitable.

By Amy Borrus



"TOUCHING A NERVE": Buchanan

### CAPITAL WRAPUP

#### NEW FOCUS ON FUJI

► The Clinton Administration may up pressure on Fuji Photo Film Co. over its ruckus with Eastman Kodak Co. The American film maker has complained to the U.S. Trade Representative's Office that Fuji unfairly dominates the Japanese market. Now the USTR wants the Justice Dept. to see if Fuji violated U.S. antitrust laws by keeping Kodak out of Japan. If Justice should intervene, it could be the first ever U.S. trust-busting case against an alleged monopoly abroad.

#### GOP FROSH: MONEY MAGNETS

► House incumbents are most vulnerable to defeat after their first term. But this year's class of 73 Republican freshmen is hauling in record mountains of cash to defend its seats. A new Federal Election Commission report shows that 15 of the top 50 House fund-raisers during the first half of 1995 were GOP freshmen. The frosh raised an average of \$123,000, vs. \$73,000 for freshmen Democrats—a bad omen for Democratic hopes of recapturing Congress in '96.

#### PAY TV?

► Broadcasters are receiving static on Capitol Hill. Congressional budget-meisters have instructed their communications subcommittees to come up with \$14 billion in revenue by 2002—when the GOP has promised to balance the budget. One likely source: auctioning off new chunks of the airwaves. That would be a huge setback for TV stations, which had expected to get new digital spectrum for little or no cost to broadcast multiple signals or lucrative data services.



## EUROPE

# SHAREHOLDER REVOLT

From Barcelona to Bonn, cozy dealings are under attack—and the balance of corporate power may shift

It was supposed to be another mega-deal, no questions asked. On Sept. 1, Fiat, Pirelli, and all-powerful Mediobanca announced that Gemina, an investment company under their control, would acquire the assets of the collapsed Ferruzzi empire. Overnight, Gemina would become Italy's No. 2 conglomerate—with the Agnellis and other magnates calling the shots.

Yet, for once, questions were asked. Minority shareholders, fund managers, and financial analysts are erupting over the Gemina deal, charging inadequate disclosure and backroom manipulation. "At this point, we've been reduced to spectators," gripes Stefano Pizzamiglio, a fund manager at investment company Finanza & Futuro Holding, which owns 3.4% of Gemina.

Europe's fat cats better get used to a permanent increase in the noise level. Their days of cozy dealings could be coming to an end as investors raise their voices. Shareholder activists are pushing companies to boost profits and dividends, oust poor management, and scrap executive-pay plans not tied to performance. They're setting up shareholder-defense committees, fighting for their rights in court, and seeking basic securities-law changes. Even Europe's holding companies, famous for their love of entrenched management, are urging companies in their portfolios to boost returns.

Corporate Europe needs the wake-up call. Minority shareholders have few rights. Assets are trapped in underperforming companies. Hostile takeovers

are almost impossible. Company reports are often opaque, if not misleading. And voting rights are stacked in favor of incumbent executives who sleep easily knowing that large blocks of their companies' shares are in friendly hands.

Yet activists can already claim a growing list of victims: Compagnie de Suez Chairman Gérard Worms, booted out in July. Marc Fournier, Navigation Mixte founder and chairman for 26 years, axed in June. Europe's latest parlor game is guessing which chief-tain will come un-

shareholder revolt will change the balance of power in Corporate Europe. One reason is the need to please a powerful new class of investors. No longer can governments and domestic institutions satisfy European companies' capital demands. Instead, companies are holding their tin cups out to such pension

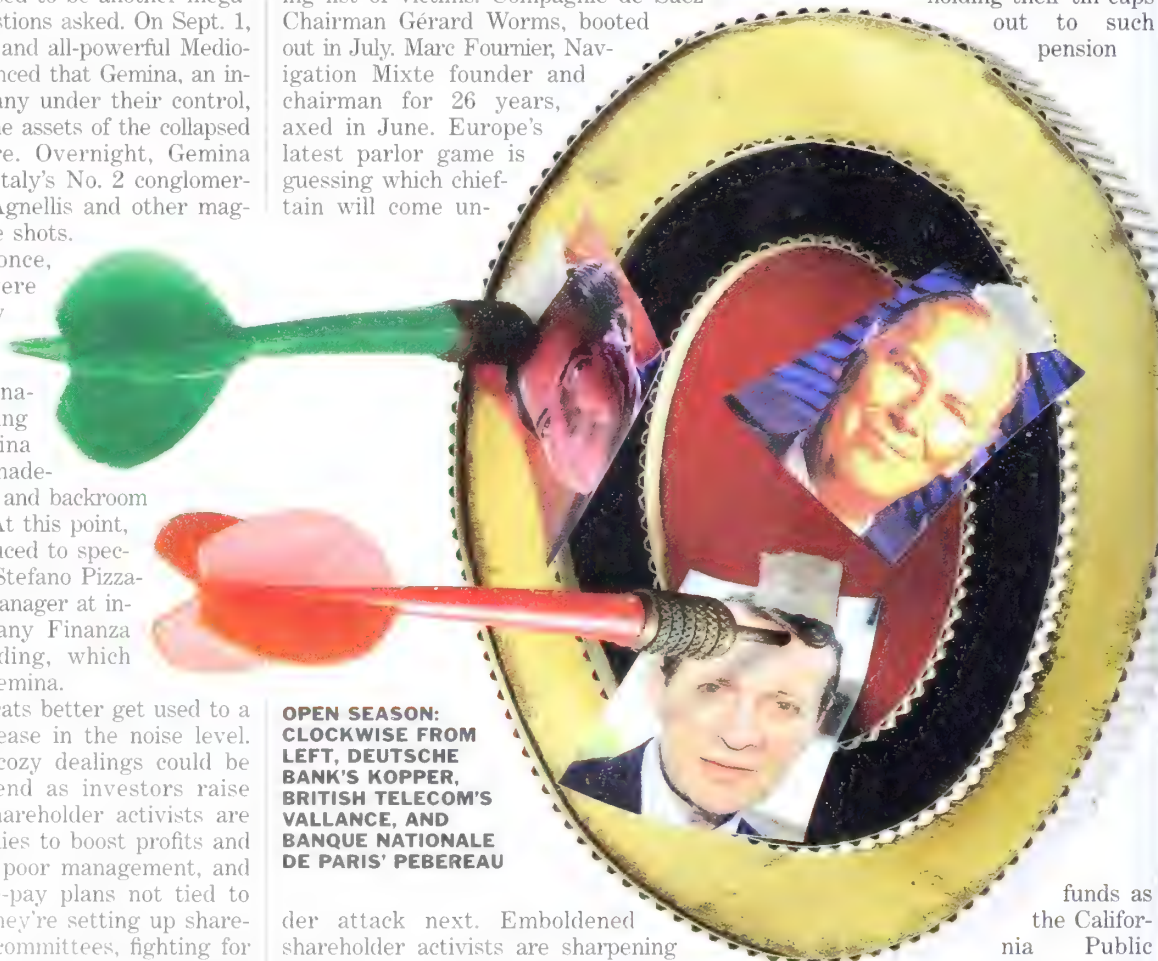
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LEFT, DEUTSCHE  
BANK'S KOPPER,  
BRITISH TELECOM'S  
VALLANCE, AND  
BANQUE NATIONALE  
DE PARIS' PEBEREAU

der attack next. Emboldened shareholder activists are sharpening their knives for some of the most powerful barons of all, including Deutsche Bank CEO Hilmar Kopper, Mediobanca Chairman Enrico Cuccia, Banque Nationale de Paris' Michel Pébereau, and British Telecommunications Chairman Iain Vallance.

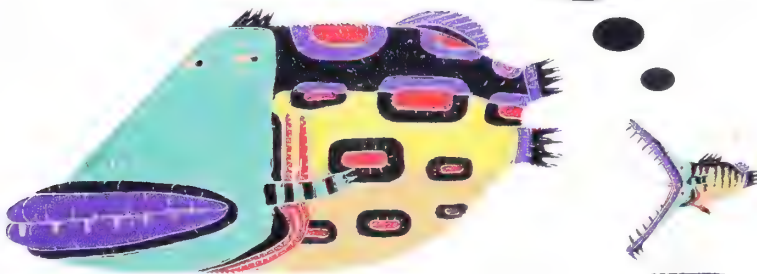
The movement is young. And so far, it has seen more defeats than victories. But if present trends continue, the

funds as the California Public Employees' Retirement System (CalPERS), which just voted to increase from \$11 billion to \$18 billion the amount it invests in European equities.

Of some \$500 billion in stock issued by Europe's newly privatized companies, about 20% went to U.S. institutions, which demand more transparency and better returns than most European



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companies have ever been subject to. Privatization has also created a small army of domestic investors, many of whom are learning to band together or to enlist the aid of shareholder activists. The result will not be a wholesale adoption of the U.S. system. But more companies will allow independent outsiders to sit on boards and question management decisions. They also will be under pressure to more openly disclose operating results, strategic goals, and even their mistakes.

The battle has recently been hottest in France. Over the past decade, France has evolved from a *dirigiste*, state-dominated system to a capitalist halfway house. The biggest companies continue to hold major stakes in one another, and a small cadre of executives dominates the system at the top, many pledging not to interfere in each other's businesses. With few pension funds and mutual funds in France to buy shares in privatized companies, the government has sold key stakes in former state companies to industrial holding companies to keep these assets in French hands.

**NO VISION.** Now, this cozy system is unraveling. In June, banking giant Compagnie Financière de Paribas, insurer Allianz, and other shareholders ousted the management of Navigation Mixte, an unwieldy \$3.1 billion holding company with interests ranging from aircraft to perfumes to orange groves, because they believed founder and longtime Chairman Fournier had no strategic vision. "We couldn't get any indication from Fournier as to where the company was going," complains Paribas Chairman André Lévy-Lang. "We were not satisfied with the status quo."

An even more monumental revolt followed at Suez, the giant of French holding companies. Chairman Worms was forced out for failing to give shareholders an adequate return on their investment, an argument rarely heard in a country where directors don't have a legally binding fiduciary duty to protect investors.

Other motives may have been at play. Observers believe that BNP Chairman Pébereau, who led the attack, most likely was eyeing Suez's Banque Indosuez, an investment bank with a valuable Asian franchise.

Ironically Pébereau may be the next target. Some insiders think another reason he was eager to get his hands on Suez was that the merger would distract attention from BNP's own troubles, including poor profitability, problems with real estate holdings, and a languishing share price since the bank's privatization. Foreign fund managers are already complaining.

not whether to change, but how much and how fast. Yet its minority shareholders can be legally treated as second-class citizens, such as when the März Group, the country's second-largest brewer, sold off a Hamburg brewery late last year. März Group got \$528 a share. But minority holders got only \$396 a share, based on an accounting report that shares were worth 25% less.

Germany's corporate boards are also under attack. At one level is the supervisory board, made up of business, bank, and union representatives. They appoint the chief executive, vet his executive nominations, and are supposed to scrutinize strategy. But they meet only once a quarter and are dependent on information fed to them by the second tier, the management board. Critics find the system too lax and blame it for spectacular scandals, including Metallgesellschaft's derivatives losses, which required a \$5 billion bank bailout.

**HOT SEAT.** Many managers point at Germany's most powerful institution, Deutsche Bank, for its failure to detect the problem. Deutsche Bank was Metallgesellschaft's largest creditor, and the bank's corporate-finance chief, Ronaldo H. Schmalz, chaired MG's supervisory board. More recently, Deutsche Bank is also been in the hot seat over a string of scandals at Daimler-Benz.

In late June, Daimler warned of severe losses for 1995, just

four weeks after predicting a rosy future at an annual meeting. The struggle is partly to blame, but some believe Daimler's problems go to the heart of the corporate-governance system. "It's all one big ingrown club, a classic old-boy network," says University of Chicago Graduate School of Business Professor Merton H. Miller, who has studied the German model. "You cover up for one another. There's no one who says 'you blew it,' and you never have to admit your mistakes."

No doubt, Deutsche Bank's hold in Germany Inc. is tight. Its board members have seats on more than 100 large

## Why Europe's Shareholders Are Up In Arms

### THE CHARGES

#### CORPORATE INCEST

Banks and companies hold large passive stakes in one another and sit on each other's boards, giving managers little incentive to boost shareholder value

#### MINORITY ABUSES

In mergers, minority shareholders often get no offer at all or a lower price than majority shareholders do

#### PRIVATE FIEFDOMS

Bosses have named family members as successors, renamed companies after themselves, and arranged deals to benefit friends

#### LACK OF TRANSPARENCY

Company statements hide major problems, from underfunded pensions to financial irregularities

#### UNEVEN VOTING RIGHTS

Forget one share, one vote—longtime and inside shareholders often get better voting rights than individual shareholders

### WHO'S TARGETED

Deutsche Bank-Daimler Benz, Suez-Banque Nationale de Paris-UAP

März Group, LaFarge-Coppée, Lagardère Groupe, Société Générale

Danone, Pinault-Printemps-Redoute, Lagardère, Laura Ashley, Mediobanca

Gemina, Daimler Benz, Banco Español de Crédito

Danone, Elf Aquitaine, RWE, Investor

DATA: BUSINESS WEEK

In the end, what's important is that cracks are opening in the *noyau dur*, or hard core, of stable shareholders that protects French managers from the ravages of market forces. Now, France's business chieftains are on notice that they, too, must watch their companies' performance or suffer the fate of Fournier and Worms. Paribas' Lévy-Lang is concerned. "I'm not satisfied and neither are my shareholders, because the share price is too low and our earnings are, too. The message we're getting is that we need more focus," he says.

Like France, Germany is debating

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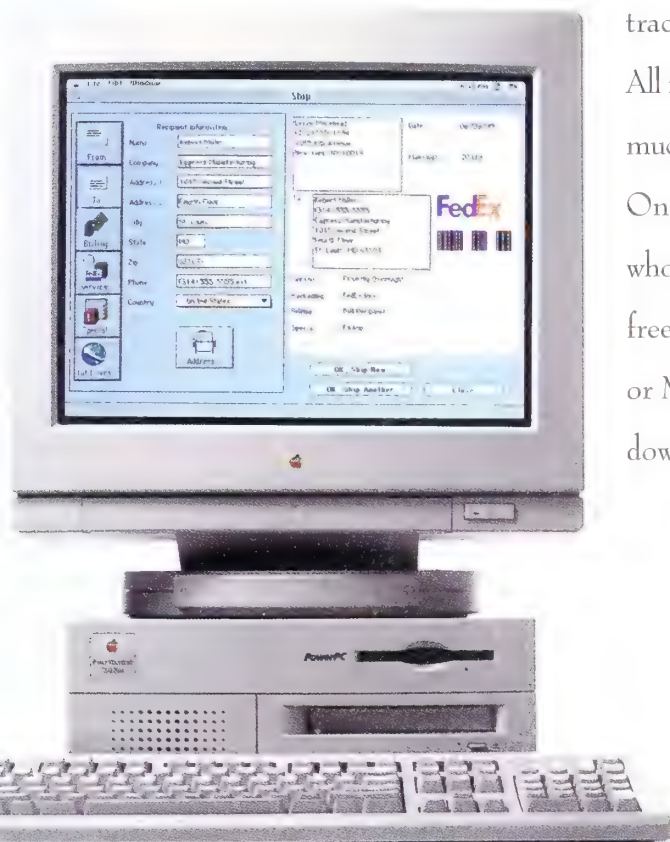
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companies in which it holds stakes, including 24% of Daimler, the country's largest company. Deutsche Bank CEO Kopper chairs Daimler's supervisory board and sits on seven other boards as well. Critics allege he can't possibly have the time to do each job well. Moreover, of the 20 executives on Daimler's supervisory board, only two have experience running a major manufacturer.

Even though Deutsche Bank failed

to prevent Daimler's missteps, its attitude toward governance issues is undergoing a sea change. It has reduced its Daimler stake, from 28% to 24.4%, and says it plans to scale back holdings in other companies as well. Its mutual-fund arm, with \$77 billion invested, now sends representatives to speak at the annual meetings of BASF, Hoechst, and a dozen others to push for better returns.

In Britain, which led Europe in agi-

tating for shareholder rights, activists are homing in on new targets. Among the big issues are pay packages and option plans executives are rewarding themselves. High on the hit list: the generous bonus of British Telecom's Vallance.

In Italy, by contrast, change is far slower than in the North. Total stock market capitalization amounts to just 18% of gross national product, compared with 130% in Britain. Despite the rising assertiveness of outside shareholders and fund managers, it will take longer to crack the iron grip that the state and a small clique of powerful industrial heads have on most of Italian industry. The system leaves the stock market undeveloped and minority shareholders powerless.

A key obstacle to reform is the secretive merchant bank Mediobanca and its 87-year-old Chairman Cuccia. Mediobanca is the hub of Northern Italy's industrial dynasties and the driving force of the private sector. It has stakes in many blue-chip Italian companies, and they in turn have stakes in Mediobanca. This web of interlocking shareholders act in concert when choosing boards and voting on management decisions, such as Gemina's takeover of Ferruzzi, which affects 30% of all shares traded on Milan's stock exchange.

**FUTURE BLOCK.** Critics allege that by grabbing shares of newly privatized banks and installing its own managers, Mediobanca is preventing Italy from reaping the benefits of privatization. In July, Italian antitrust authorities launched a probe into whether Mediobanca is hindering competition. Mediobanca would not comment.

Clearly, Europe is only in the early stages of what will be a long campaign to bring its corporate oversight up to the expectations of global investors. That may mean taking painful steps, such as changing accounting practices, laying off workers, and moving production outside of the country.

It will also mean revealing treasure secrets, as Jérôme Monod, chairman of France's Lyonnaise des Eaux has decided to do. With 28% of his shareholders outside France, Monod announced on Sept. 4 that he will publish his salary and stock options in the company's annual report beginning next spring. That a leading French executive has taken such a step proves that Europe's shareholder revolt is far more than a fleeting trend. It is penetrating the inner sanctums of Europe's corporations.

By Paula Dwyer in London, with Christina Bennett in Rome, Marshall Johnston in Paris, Julia Flynn in London, and Karen Lowry Miller in Bonn

## CITOYENS! TO THE CORPORATE BARRICADES!

If the lofty executives who run France's old-boy companies are taking more notice of shareholders, it's due largely to a petite, 58-year-old economist named Colette Neuville. From her 19th-century farmhouse near Chartres, where she lives with her retired civil-servant husband and several cats, Neuville is campaigning to force new account-

The cream of French business has come under Neuville's attack, in and out of court: Pinault-Printemps-Redoute, Euro Disney, and Banque Paribas-Stern. Mistreatment of minority shareholders in takeovers is a common complaint. Her campaigns have led regulators to tighten takeover rules, and executives credit her with making *le corporate governance* an is-



### COLETTE NEUVILLE

She has attacked the elite of France Inc. Takeover rules, as a result, have been strengthened

ability on a reluctant France Inc.

The feisty mother of five jumped into the governance game in 1990, when a Paris brokerage that held her modest stock account went broke. She formed an association to rescue small clients' savings. It snowballed into France's first big shareholder advocacy body: the Association for the Defense of Minority Shareholders.

sue. Recently she was named a director of the investment bank Paribas.

Crusading is Neuville's second career. She did economic research for a French tiremaker and NATO before staying home for 20 years to raise her children. She owns few shares herself, she says, because of her modest means: "We live off my husband's pension, and I travel second-class with a family discount." She'll never get French executives to follow suit. But as France's godmother of governance, Neuville is forcing fresh air into a musty system.

By Stewart Toy in Paris



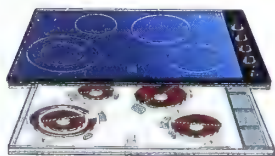


The prudent acorn woodpecker bores small holes in trunks of dead trees to store an adequate food supply for the cold winter months to come.

Nature teaches creatures to provide for the future. It's an essential precaution for the acorn woodpecker. It's also an important lesson for today's industries. A company's success depends on its ability to identify future needs and invest well ahead of time.

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## ASIA

### FORD OPENS THE THROTTLE

It's challenging Toyota's dominance in the Far East

**E**xecutives of Ford Motor Co. were making great progress negotiating to build a factory in Vietnam on a site east of Hanoi. Then the Americans made a startling discovery: The location would be a rice paddy during growing season and would be under water.

But Ford managed to resuscitate the \$102 million deal. It quietly persuaded the government to prevent farmers from growing rice in the area and came up with a way to build a plant on soggy ground. On Sept. 6, Vietnamese Prime Minister Vo Van Kiet gave the green light to Ford's joint venture, along with a separate deal for Chrysler Corp.

Ford's struggle to establish an outpost in Vietnam is part of the auto maker's boldest grab ever for market share in Asia. After lagging behind the Japanese and even its Detroit rivals in Asia's emerging markets, Ford is now spending \$1 billion to set up factories in China, India, Thailand, and Vietnam (table). Ford already has joint ventures in Taiwan and South Korea, in addition to a presence in Japan.

**ROUGH RIDE.** But it is the newest markets that offer the greatest allure. The sudden surge into those countries is part of Ford Chairman Alexander J. Trotman's ambitious global strategy. Just as Trotman is aiming to topple General Motors Corp. in North America, he is setting his sights on Toyota Motor Corp. in Asia. "We clearly want a presence

in Asia that is equal to Toyota, if not higher," says W. Wayne Booker, Ford's executive vice-president for international automotive operations.

Booker is in for a rough ride, particularly in Southeast Asia, where Japanese auto makers control 90% of the market. In all of Asia, Toyota now sells one out of every four vehicles on the road, while Ford has only a 2.5% sliver



**BIG AMBITIONS:** Booker predicts profits within five years

of the market. But expanding that foothold is crucial because while auto markets in Europe, North America, and Japan are barely grinding upward, the emerging Asian market is growing up to 20% a year.

To catch up, Ford faces tricky challenges in picking the right business partners and gaining the management knowhow to operate in Asia. "The Jap-

anese today have all the first-comer advantages in Asia, and the Americans have all the latecomer disadvantages," said Linda Y.C. Lim, a University of Michigan specialist on Southeast Asia.

Ford does have a Japanese card of its own to play because of a 25% stake in Mazda Motor Corp. Ford is relying on that relationship to build a \$500 million joint-venture factory in Thailand. The venture, which will begin producing Mazda-designed small pickups in 1998, is tailor-made for the fast-growing Thai market. Ford uses the Mazda connection in Malaysia and Indonesia as well.

**SWEATY SHOP.** But Ford also wants to assert its own identity. That will require even more investments to build a full-fledged presence in key markets. Ford's dealings in China are an exam-

ple of how the company is trying to do that. "Anyone who wants to be a player must be involved in China," says Trotman, who visited Shanghai in late August, his third trip to China this year. Ford has dealings in that city with ultrasuccessful Shanghai Automotive Industry Corp. (SAIC), which is involved in joint ventures with several different foreign companies.

In one venture, Ford is trying to help reorganize and modernize some older plants at Shanghai Yanfeng Automotive Trim Co., which is controlled by SAIC. In one factory built in 1971 there is little hint of modern efficiency as employees stand idle waiting their

turn to pump liquid polyurethane into a car-door mold. Steering wheels, sun visors, and instrument panels also are made in this crowded factory.

Meanwhile, on the other side of town Ford is doing many of these same operations but in Yanfeng's youngest plant built in 1991. It has three times the space and much more modern machines. Ford will double its initial investment o

**Ford's  
Push into  
Asia's  
Newest  
Markets**

DALE GARNER/REUTERS

#### CHINA

Paying \$40 million for a 20% stake in Jiangling Motors, which will make Ford trucks and vans. Already spent \$200 million on four parts plants near Shanghai.

#### VIETNAM

Investing \$102 million in a joint venture with Song Cong Diesel to build an auto assembly plant just east of Hanoi. Sales and service arms being established.

#### THAILAND

Forming a \$500 million joint venture with Mazda Motor to build a pickup truck factory southeast of Bangkok, with production to start in mid-1998.

#### INDIA

Spending \$50 million to acquire a 7% stake in Indian auto maker Mahindra & Mahindra. An \$800 million assembly plant will produce Ford-designed small cars.



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## CHINA

### COUNTERFEIT DISKS, SUSPECT ENFORCEMENT

China's feeble piracy crackdown puts Clinton in a quandary

\$70 million in the factories over the next three years, says Yanfeng General Manager Robert Bertsch. In short, Ford is entering traditional joint ventures with key Chinese companies—thereby pleasing a demanding Chinese government and building *guanxi*, or connections—while working hard to modernize and expand those companies.

Despite its newcomer status, Ford displayed savvy in the way it bought into Jiangling Motors Co. in a separate deal. In August, it announced it would buy 20% of the company when the shares are floated on the Shenzhen Stock Exchange. Western analysts say the company has financial difficulties, but Ford argues it has achieved a long-term production deal, bypassing any central government decision-making process. The two companies plan to produce a light pickup truck, passenger bus, and van by 1997.

**FULL PLATE.** Ford could consolidate its position in China by winning a role in developing and building a luxury sedan that Shanghai authorities want to announce by the end of the year. General Motors is vying for the deal, but Ford is getting some early breaks. SAIC, tightly controlled by Shanghai city authorities, will be the producer of the sedan. That means Ford has a crucial working relationship with the key Chinese player.

Will the Great Asian Push pay off? The burst of Ford deals already has some on Wall Street worried that the auto maker will sacrifice the bottom line in pursuit of global dominance. "They have an awful lot on their plate right now," says analyst David Healy of New York-based Burnham Securities Inc. "Investors hope this growth does not come at the expense of profitability."

Booker promises that Ford will be earning profits on its Asian investments within five years, but rivals scoff that it could take longer. "I wish them luck," says Tom McDaniel, who was vice-president of GM's Asian operations from 1989 until this year.

But despite the pitfalls—including rice paddies that double as plant sites—Ford is determined to win in the emerging Asian economies. Those hotly courted Vietnamese consumers purchased only 11,500 vehicles last year, a mere two weeks' worth of output from one of Ford's American factories. But in Ford's new, expansionist view, Asian consumers hold the key to helping it become the world's largest auto maker.

*By Keith Naughton in Detroit, with Dexter Roberts in Shanghai, Ken Stier in Hanoi, and bureau reports*

It's back-to-school time in Beijing's Zhong Guan Cun district, and students, teachers, and others are out for a last Saturday of shopping. Bargain hunters compare prices in the neighborhood's many small computer shops selling gear made by Compaq, IBM, Epson, and Hewlett-Packard.

But on a corner just minutes away, throngs of people are eagerly jostling for some illicit bargains. Pirated copies of Microsoft Corp.'s Bookshelf 95 multimedia reference library and Art Gallery, London's National Gallery collec-

and music recordings feeds America's bulging trade deficit with China. With the trade gap heading for \$40 billion this year, Beijing's failure to halt intellectual-property theft makes for tempting political fodder at home.

**JAIL TIME.** The toll on U.S. business is high. Trade groups estimate that bootlegging in China cost almost \$870 million in lost sales in 1994. This year's losses could match or surpass that level, thanks to an apparent surge in Chinese production of pirated CD-ROMs.

China has taken some steps in the right direction. Since the accord was struck in February, authorities have conducted more than 3,000 raids and confiscated millions of illicit items. Convicted peddlers of bootleg goods now face stiff fines and time in jail.

But profit margins as high as 40% continue to lure dealers onto the streets. Despite its crackdown on retailers, China has failed to shut down the factories that churn out ripoff products. Says Stephanie Mitchell, a Hong Kong-based vice-president of the Business Software Alliance: "We're on the one-yard line—with 99 yards to go."

Authorities in Beijing say they want to combat the piracy.

But their clout in the booming coastal provinces has diminished as local officials manage their own economic affairs. "It's not a matter of lacking will but lacking the ability to enforce," says Greg Mastel, senior fellow at the Economic Strategy Institute in Washington.

Trade negotiators hint that the U.S. will block China's admission to the World Trade Organization until the Chinese do a better job of combating piracy. Washington also intends to ratchet up the pressure quietly through a series of visits by U.S. negotiators, starting in October. If that doesn't do the trick, the Americans may threaten sanctions again. In a Presidential election year, the Administration can't afford to let this potential trade victory turn into defeat.

*By Amy Borrus in Washington, Dexter Roberts in Beijing, and Joyce Barnathan in Hong Kong*



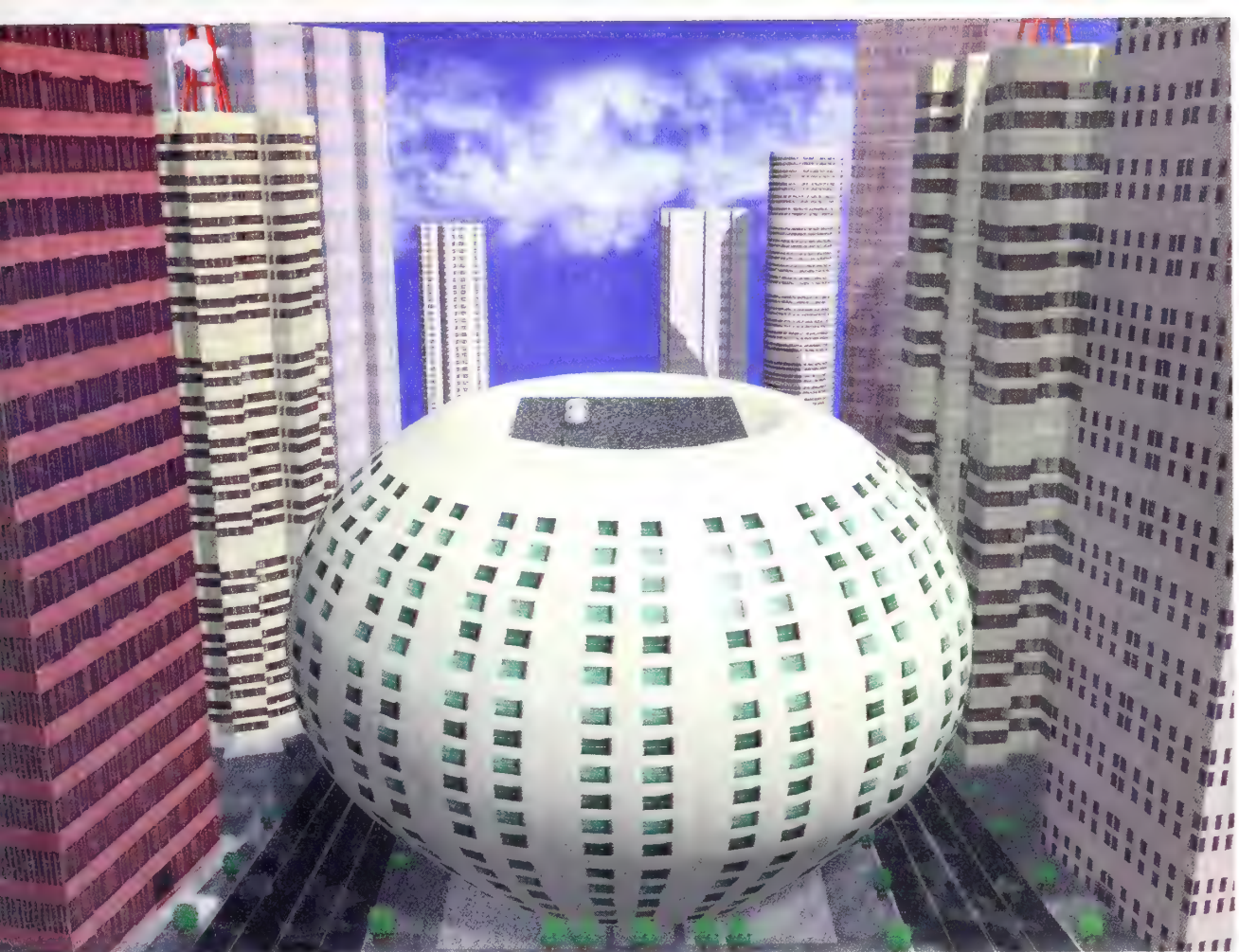
**"PSST!"**  
Six months after  
an antipiracy  
pact, little seems  
to have changed

tion, each sell for \$6, while Windows 95 copies are selling for just \$4. "You better buy now before the next crackdown," says one dealer.

Such scenes speak volumes about the difficulties the U.S. faces in getting China to enforce a six-month-old accord aimed at stamping out piracy of intellectual property. While there has been "a significant change in the Chinese government's attitude," says a senior U.S. Administration official, "on the ground, the picture is mixed."

Trouble on the trade front is the last thing the Clinton Administration wants as it tries to mend the badly frayed Sino-U.S. relationship. But counterfeiting of U.S. software, movies, books,





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EDITED BY STANLEY REED

## THE GREEN WHO WOULD BE GERMANY'S KINGMAKER

**G**ermany's Green Party has long had a reputation for tree-hugging idealism, but under their new Bundestag leader, Joschka Fischer, the Greens are now trying to make the huge leap from gadflies to power brokers. "There's no point in being in politics if you don't get into power," the telegenic Fischer, 47, tells the thirtysomethings and ex-hippies, who form the party's backbone.

The Greens' goal is to replace the centrist Free Democratic Party (FDP) as the third force in German politics—behind Chancellor Helmut Kohl's Christian Democratic Union (CDU) and the Social Democratic Party (SPD). In an effort to win over young professionals, the Greens are moving beyond strict environmentalism. They are pushing to curb automatic entitlements and to cut government bureaucracy. Recently, they said that the state of Lower Saxony should sell its 20% stake in Volkswagen to slash the interest payments on loans used to finance that holding.

**"DRESS REHEARSAL."** But if the Greens succeed, Germany's political center of gravity will shift sharply leftward. The FDP, which backs free-market capitalism, has been Germany's kingmaker for a generation, wielding influence far beyond the 7% to 10% it won in national elections. But the party is now in steep decline. The Greens are outpolling the FDP nationally, and in last May's elections in Germany's most populous state, North Rhine-Westphalia, the FDP failed to clear the 5% threshold for seats, while the Greens, who won 10% of the vote, wound up in a ruling coalition with the SPD. "It's a dress rehearsal for national power," says political consultant Heinz Schulte. "North Rhine-Westphalia is where general elections are won and lost."

Indeed, the SPD's embattled leader, Rudolf Scharping, now apparently sees cooperation with the Greens as his best shot at unseating Kohl, who has doggedly hung on to power since

1982. Scharping, who is slipping in the polls, had been adamantly opposed to sharing power with the Greens but now calls the North Rhine-Westphalia arrangement a test of "the potential" for a national coalition with them.

Having won this much respectability, Fischer, whose cohorts have 49 of the 672 Bundestag seats, is doing his best to persuade skeptics that they can trust him. He argues that environmentally friendly industry will create jobs in such areas as pollution control. He also promises that a huge proposed

energy tax, which would more than double the price of gasoline, to \$11.50 per gallon, would be revenue neutral. Says consultant Schulte: "[The Greens] are prepared to sell their soul for seats in the next government."

**EASTERN RADICALS.** The Greens are having some success in at least softening the criticism of business chiefs. Fischer, for instance, seems to be establishing a working relationship with Hans-Olaf Henkel, former CEO of IBM Deutschland and now president of the Federation of German Industry. Henkel had been critical of the Greens' program, including a move to a 30-hour workweek, a legal ban on overtime, and imposition of speed limits on the currently unfettered autobahns. But now one of his aides says of the Greens: "In recent weeks, many of their statements have been moderate and pragmatic."

Still, many business leaders worry that Fischer will be undercut by party radicals, particularly those from east Germany. A major showdown seems likely at the party congress in Bremen in December. Militant Greens known as "Fundis" don't want to abandon cherished demands, including immediate shutdowns of nuclear plants and autobahn speed limits. "Realos" like Fischer say they want to continue pursuing environmental goals but to be more flexible in reaching them. If the pragmatists lose, then Kohl can sleep easier.

*By John Templeman in Bonn*



**FISCHER:** *Besting the FDP*

### GLOBAL WRAPUP

#### A NEW MODEL FOR RUSSIA?

► In a move that could have far-reaching implications, President Boris Yeltsin is going ahead with a novel deal in which nine Russian banks will lend the government about \$2 billion in exchange for state-owned shares of some 100, yet-unnamed companies. This could mark the beginning of an emerging economic structure similar to Germany's or Japan's in which banks have close ties to big business.

The scheme is aimed at giving the

hard-pressed Kremlin budgetary relief. Anatoly B. Chubais, the Deputy Prime Minister in charge of economic policy, says foreign firms are welcome to take part in the loan, but their initial interest appears lukewarm. Special restrictions will supposedly keep the banks from stripping company assets or making big changes in management.

#### ISRAEL FINDS DEFENSE WORK

► Turkey has selected Israel Aircraft Industries Ltd. to improve the avionics and otherwise upgrade its fleet of

aging American-made Phantom jet fighters. The cost of the project is put at \$600 million dollars. IAI and other Israeli companies have been extremely aggressive in the military-upgrading market in an attempt to offset a decline in defense sales. IAI has already won contracts from Australia, Chile, and the U.S. Air Force, and the company is working on Soviet-built MiG-21s for several Eastern European and Asian countries. In order to clinch the deal with Turkey, Israel had to agree to defer payment for two years.

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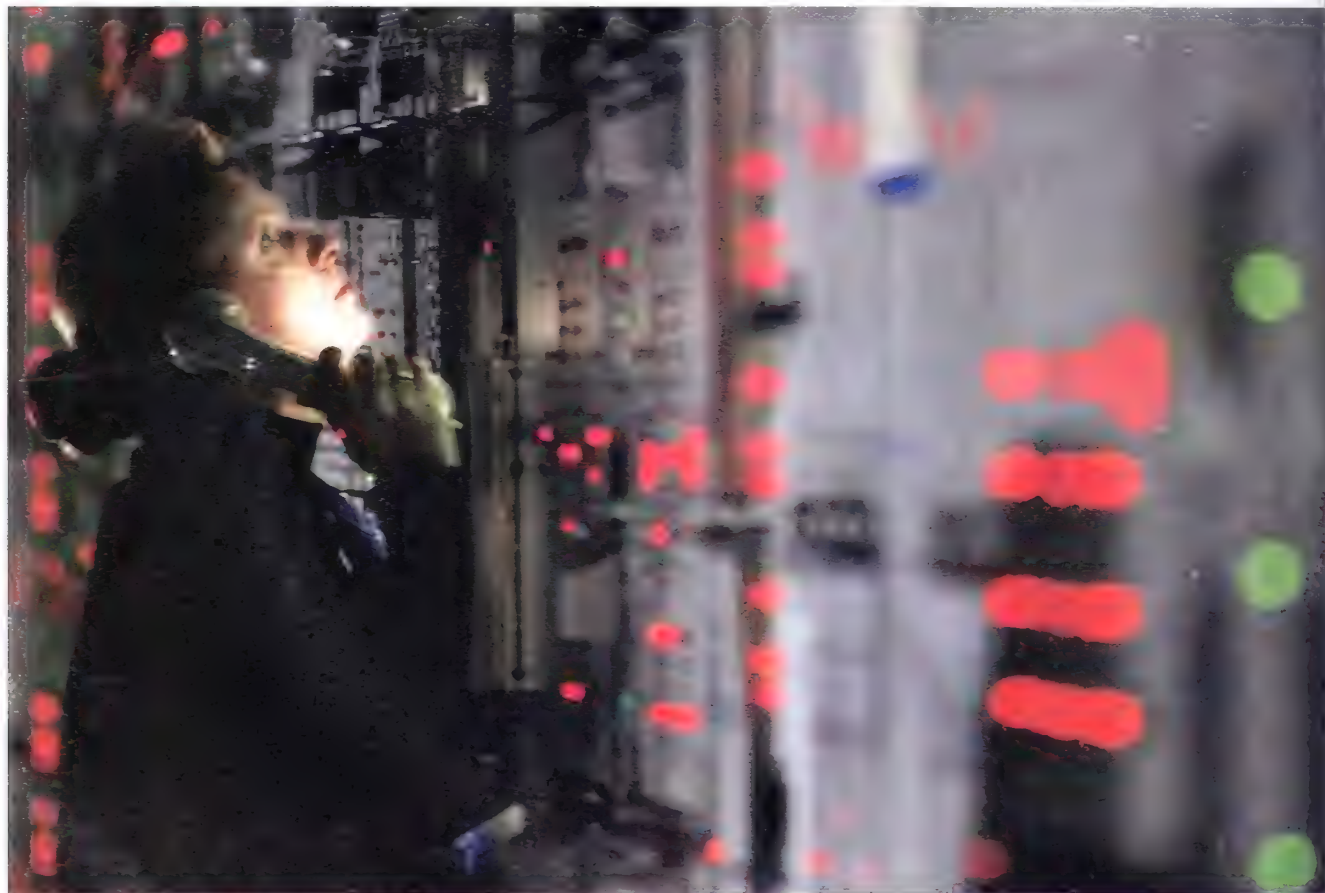
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# WHO'S AFRAID OF GLOBAL MARKETS? NOT U.S. INVESTORS

Although foreign equities are volatile, even stodgy institutions are buying big stakes



**A DEUTSCHE TELECOM TECHNICIAN:** *The company's IPO will be a landmark event for U.S. investors.*

**T**he rumblings between China and the United States over the recent trade dispute have been a familiar sight. You would think U.S. institutional investors would be running for cover. But they are not. They are still in the haven of home-grown blue chips and the past.

That putting all of their eggs in a domestic basket is ultimately riskier, U.S.

search of portfolio diversification and growth. Moving the spotlight on the globalization of American industry, U.S. portfolio investments are expanding so rapidly that they now account for 12% of the nation's \$9 trillion in pension and mutual-fund assets, the International Monetary Fund estimates, up from under 5% in 1991. In the past five years alone, U.S. investors have poured more than \$330 billion into stocks and bonds from Toronto to Taipei (charts), according to the Federal Reserve Board.

That share will almost certainly keep rising. International securities are al-

ready a mainstay of Wall Street's investment banks—and Main Street's portfolios. Thousands of international companies trade on U.S. markets as American depositary receipts, and large quantities of international equities have even become fundamental parts of many domestically oriented mutual funds. Some pension funds, including that of the Illinois teachers' retirement system, have invested over 20% of assets abroad.

**GOING OVERSEAS.** With Germany, China, Mexico, and a host of other countries planning to offer American investors the chance to take part in huge

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privatizations over the next few years, the rush to overseas funds shows little sign of abating. By 2000, estimates InterSec Research Corp., a financial consultant in Stamford, Conn., U.S. pension funds' international assets will reach \$725 billion, more than double what they are today.

U.S. pension and mutual funds are going overseas for sound economic reasons. Many investment experts believe that only through globalization can American institutions achieve the portfolio diversification they need to provide a generous long-term return without taking inordinate risk.

It's no wonder, then, that a recent Greenwich Associates survey of 1,620 U.S. pension funds managing \$2.7 billion in assets found that 65% already invest abroad—and 28% more plan to do so shortly. The consultant, based in Greenwich, Conn., found that 17% of the funds play the emerging markets—and they are sticking by their investments despite the sector's blowout earlier this year.

**SHOCK WAVES.** Look at the performance averages, and it's no surprise money managers are staying the course. Global investing has paid off even in the face of periodic bubbles and panics on world markets. Over the past 10 years, InterSec Research estimates, U.S. pension funds earned a compounded annual return of 18.2% on overseas investments. That's nearly four percentage points greater than what the funds would have earned by investing in the overwhelmingly domestic stocks that make up the Standard & Poor's 500-stock average. "U.S. investors are finally convinced that 'international' is something that belongs in their portfolios," says InterSec Director James A. Diack.

To be sure, massive flows of cross-border capital can cause upsets, as the turbulent markets of 1994 dem-

onstrated. Last year, when the Federal Reserve sharply hiked interest rates to head off inflation, many investors shifted capital back to America to seek rising yields. That—and the subsequent Mexican debacle—sent shock waves through Latin America, Asia, and Eastern Europe. Baring Securities International Ltd. strategist Michael J. Howell estimates that the interest-rate reversal caused the flow of U.S. portfolio capital abroad to plunge from 1993's record \$437 billion to \$233 billion in 1994.

In another sign of the punch that U.S. money flows can pack overseas, foreign companies must pay increasing attention to pleasing American investors. That has brought a new discipline to management. As global investors demand more uniform standards of corporate accounting and disclosure, many foreign companies must learn to meet

the close scrutiny of those who provide their capital.

For example, James Hatt, British-born CEO of Petersburg Long Distance Inc. (PLD), spends most of his time overseeing his telephone company's operations in the former Soviet Union. But every few months, Hatt makes a crucial trip to the U.S. After Toronto-based PLD raised \$98.4 million last year via a stock offering on NASDAQ's over-the-counter market, Hatt soon learned that he would regularly have to make the rounds on Wall Street to keep his stockholders up to date.

The sheer weight of U.S. money flows is also putting pressure on companies to deliver satisfactory returns on equity. Take giant Deutsche Telekom, the German phone monopoly slated for privatization in 1996. If it wants its estimated \$10 billion initial public offering

## TIGHTER LEASH Investors' demands for more uniform corporate accounting and disclosure are bringing new discipline to management at many foreign companies

to succeed, Telekom must win over foreign investors—especially Americans, the world's biggest buyers of stock.

In Germany, where most investors don't buy equities, the market is far too small to absorb Telekom's shares. So the company will have to show the kind of profit projections that make U.S. stock analysts write "buy" recommendations. To do that, the company must slash its staff, improve management, and deliver returns comparable to those of fast-growing private phone companies elsewhere. "There's a general perception that Deutsche Telekom is a very badly managed company," says Mark Breedon, manager of the New York Stock Exchange-listed Global Privatization Fund. "International investors will have to believe efficiencies will be gained, or else they won't buy."

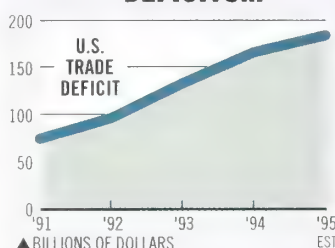
**RAFT OF PRIVATIZATIONS.** Edward McMillan of Denver money manager Bee & Associates Inc. calls this phenomenon "the globalization of value." The world is inexorably moving toward a single investment standard. And because Americans are the ones moving the most cash abroad, that standard will probably be dictated by U.S. money managers.

Even if it takes years, the transition will only further whet Americans' appetite for far-flung investments. After last year's emerging-market debacle, U.S. investors have resumed shifting cash offshore.

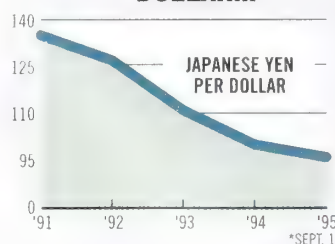
In 1995, U.S. portfolio outflows should rise to \$330 billion, figures Baring's Howell. And why not? Brazil, for example, is planning a raft of privatizations. So are several countries in Europe. Even Canada is selling railroad assets to raise cash. Despite the inevitable crashes and rebounds, the U.S. is sure to be in on these opportunities in a big way. With proof in their pockets that taking risks abroad pays off, for American investors, there's no turning back.

*By William Glasgall in New York*

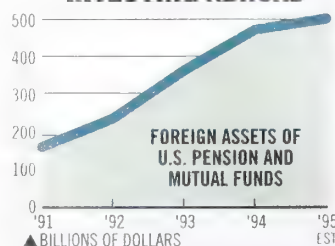
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### ...AND THE WEAK DOLLAR...



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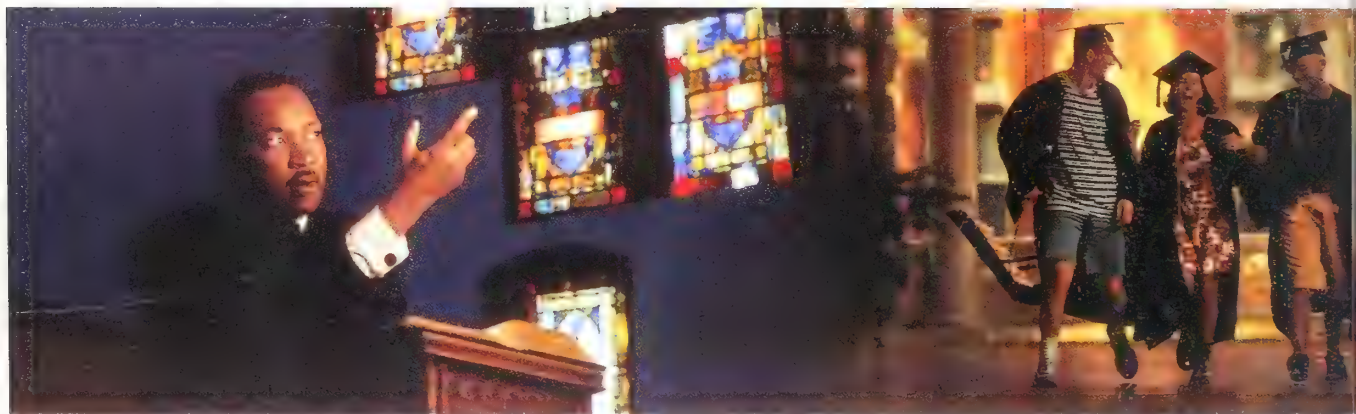


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## EUROPE

# NEVER MIND THE UGLY AMERICANS

Asians and other new-money tourists are flocking to Europe

**L**aura, a 27-year-old Japanese woman from Fukuoka, is shopping in a shop. Yumi Yamada, 27, stands happily surveying her purchases. Near the entrance of the shop, a Tokyo-based stewardess, Yamada headed straight to Rome this summer after hearing about how the sinking lira has made Italy a shopper's dream. "Things are cheaper now. My favorite thing about Italy is the shopping," Yamada says.

Yamada isn't alone in appreciating the benefits of weak currencies. In fact, this summer's price-sensitive vacationers have helped boost tourism to post-gulf-war records in Britain, Spain, and Italy, where currencies have slumped against the yen and the German mark this year. Even though business is flat in France and Germany, the European tourism industry overall is thriving. Airlines are reporting record numbers of passengers. Hotel occupancy is up 5% across Europe. The number of overseas visitors is set to surpass even last year's record of close to 20 million, says Robert A. Hollier, executive director of the European Travel Commission.

Currency is just one reason for Europe's tourist boom. Another is new wealth in emerging markets in Asia and Eastern Europe. As disposable incomes rise in countries ranging from South Korea and Taiwan to Russia, travelers are heading west. Rich Russians are plunking down cash to buy houses on the Costa del Sol. Tour groups from Indonesia, Korea, Taiwan, and Malaysia hustle to catch a glimpse of Big Ben

**"BUY, BUY, BUY."** And Eastern Europeans are swarming the Adriatic beaches. "They arrive by the busload, stay in luxury hotels. They eat, they drink, and they buy, buy, buy," says Gianfranco Donati of the Rimini Tourist Agency. An estimated half million Russians and Eastern Europeans have come to Adriatic coastal towns so far this year, a jump of about 300% over last year.

Asia and the former Soviet bloc to keep its industry growing. As tourists from the U.S., Japan, and other developed

countries head for more exotic destinations in Asia and Latin America, Europe's share of the world tourism business is shrinking. Its \$150 billion in tourism revenues last year was 47% of the world total, down from 53% five years ago.

Most of Europe's growth will come from Asia, industry sources believe. More than 800,000 non-Japanese Asians came to Europe last year. While the numbers don't yet rival the crowds from Japan, which dispatched 1.6 million visitors to Europe in 1994, they are growing in the double digits. With airline departures worldwide from Asia already increasing 15% a year, "the growth potential is enormous," says Linda Tuttle, head of the Asia Pacific Dept. at the British Tourist Authority.

Business from Korea is especially strong. When restrictions on travel and foreign currency export were eased in the late 1980s, Koreans initially jetted off to nearby Asian destinations such as Thailand and Japan. Now, they are heading to Europe. "It took Koreans a

little while to open their minds to Europe," says the Reverend Kim Ji Yoon, 28, as she races through the British Museum with a Korean tour group.

**COATS AND ROCKS.** The number of Koreans visiting Europe will grow some 30% this year, to \$20,000, according to Korean Airlines Co. Many come on 10-day, five-city whirlwind tours. And they spend. They buy Burberry coats in London, cosmetics in France, and even diamonds in Amsterdam. In Britain last year, they spent \$1,035 per visit, less than the Japanese but more than most

Americans. "Korea is following the same pattern as Japan, only 10 years later," says ETC's Hollier. "Korea could well be the source of the next big boom."

The Chinese will be close behind. China sent 40,000 visitors to Europe last year. Their numbers are expected to rise 18% a year until at least 2000 as the Chinese middle class grows and the government further eases travel restrictions.

To lure more Asians to their countries, European airlines and tourist agencies are stepping up their marketing in the region. The British Tourist Authority now spends the largest chunk of its marketing budget in Asia. The Dorchester hotel in London's fashionable Mayfair district has boosted its promotional trips to Jakarta, Hong Kong, and Sin-



QUEEN FOR A DAY:

An Asian traveler

gapore. And France's tourist board recently opened a new office in Taipei.

Their goal is to attract more tourists such as South Korean's Mi Ji Lee, 32. Soaking up the ambience near Rome's Trevi Fountain, she says: "This is my first trip to Europe. For all the beautiful paintings and sculptures I've seen, it's worth the price." The airlines, hotels, and tour operators hope she'll come back for more.

Christina Bennett in Rome and bureau reports



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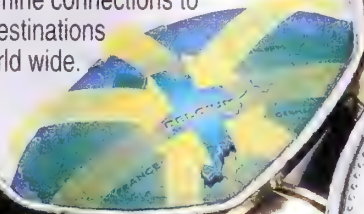
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## CHILE

# DUELING PIPELINES IN THE ANDES

Tenneco and Nova both want to supply Chile's power grid

José Yuraszek is chairman of Empresa Nacional de Electricidad (Endesa), Chile's biggest electric utility, but he also had ties to a gas pipeline consortium that included Houston's Tenneco Inc. Because a rival consortium was bidding for a critical contract to sell gas to Endesa, Yuraszek excused himself from his company's board meeting on July 12 in Santiago. To his surprise, the board voted to buy gas from the competing group, led by Calgary-based Nova Corp., which plans to build a \$285 million pipeline over the Andes from Argentina. "It was a rout," says Yuraszek.

But Tenneco and its partner, British Gas PLC, are not giving up. Despite Nova's coup in signing up Endesa, which produces 60% of Chile's electricity, they are pushing ahead with a longer, \$700 million pipeline from Argentina. They will compete head-on against Nova for customers around Santiago and also will supply a nascent industrial corridor in central Chile.

**SOUTHERN CONE.** It's a high-stakes battle. If both pipelines are built, there almost certainly will be a years-long energy glut, lower prices for gas and electricity, and diminished profit margins for gas suppliers and power generators alike. "In my mind, there is no room for both projects," says Rafael Quijano, a Latin America analyst at Washington-based consultant Petroleum Finance Co.

But the incentives on both sides to push ahead are powerful. The pipelines and new power plants they will supply are admission tickets to Chile's fast-growing energy market, which has been supplied mainly by hydroelectric and coal-fired plants.

Looking ahead, the rivals foresee a

day when the entire Southern Cone—Chile, Argentina, Brazil, and neighboring countries—will be supplied with energy from a vast gas basin stretching along the Andes' eastern flank from Argentina to Peru. Nova already has a stake in an Argentine gas pipeline, TGN, while Tenneco and British Gas are among the

any other time," observes Ewell H. Muse III, senior vice-president of Tenneco's gas subsidiary and president of TransGas.

Some analysts speculate that the two pipeline projects will have to merge, but both sides dismiss the prospect. "We're not interested in their project," says Muse. Adds Nick J. Kangles, a senior vice-president at Nova: "There has been talk [of merging] in the past, but it has been unproductive."

**TIGHT SCHEDULE.** Chile's government has decided against intervening in the fight. Officials had worried that competition could be dampened by the membership of electric utility holding company Enersis, a major shareholder in Endesa, in the original TransGas group. But Enersis dropped out of the project after Endesa decided to buy from Nova. Tenneco and British Gas then hastened to reassure the government that they had no plans to get into the generating business.

Nova promises to start deliveries

by May, 1997, taking gas from its Argentine pipeline affiliate. In order to meet the target, Nova's Argentine and Brazilian contractors must start work by Nov. 1 in order to have two Southern Hemisphere summers for pipe-laying over an 11,500-foot Andean pass. "It's a race," says

Kangles. "Our construction schedule is ahead" of the TransGas plan. Retorts John Enloe, a senior vice-president of British Gas: "It's not who starts first, it's who can deliver gas in 1997." TransGas is planning to start work next May and hopes to begin deliveries in September, 1997. Along its route through central Chile, it plans to spend \$30 million to help 100 prospective industrial customers convert their plants to gas in return for four-year contracts.

Even with two competing pipelines, Muse says, TransGas will earn a profit above 11%—the rate of return that U.S. regulators would allow, he calculates, for a comparable project in the U.S. But if the slugfest keeps profits close to that minimum, the rivals will be poorly compensated for their risk-taking. In that event, the only sure winners will be Chilean consumers of cheaper energy.

By Susan Jackson in Santiago

## WHO WILL WIN THE PRIZE?



### FRONT RUNNER

Calgary-based Nova hopes to preempt the market with its plan to start construction in November on a \$285 million, 290-mile pipeline to supply gas to Santiago. It will tap into an existing pipeline of Argentine consortium TGN.

PARTNER: Chilgener

### CHALLENGER

Houston-based Tenneco, refusing to cede the market, plans to start work in May, 1996, on a \$700 million, 500-mile pipeline to carry gas from Argentine fields to Santiago and central Chile.

PARTNERS: British Gas, ENAP, Argentine gas producers

partners in a proposed \$2 billion pipeline from Bolivia to Brazil.

That sense of opportunity is also attracting U.S. electric utilities. In late July, the Tenneco-British Gas partnership, called TransGas, announced that it will be supplying gas to plants to be built in central Chile by New Orleans' Entergy, Atlanta's Southern, and Boston-based International Generating (Intergen), which is owned by Bechtel Group and Pacific Gas & Electric. Southern and Intergen already have Chilean investments. "If [U.S. power companies] don't get into Chile's central grid this year, they probably won't at

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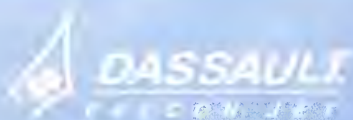
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## FALCON 900B AND 900EX



# HONDA'S CIVIC LESSON

The carmaker learned to listen to the troops when a key model faced a cost squeeze



By rights, late 1991 should have been a time of triumph for Ron Shriver. The Honda engineer, then 33, had just helped launch all-new 1992 Civic at the company's Liberty (Ohio) factory. Already, magazines and enthusiastic buyers were showering praise on the spunky subcompact. "Honda has achieved pole position in the small car sweepstakes," declared *Car & Driver*. But instead of celebrating, Shriver was worried. Slick new features such as rear-seat heat vents and a beefier engine had hiked costs just as auto sales were slumping in the U.S. and Japan. American car buyers were balking at prices that topped out at \$15,000, the yen's relentless run-up against the dollar showed no signs of slowing. Honda Motor Co.'s profit margins, already razor-thin, looked as if they would disappear. So even as the first 1992 model-year Civics were hitting the road, Shriver put together a 12-member team

that would spend the next 18 months scouring Honda's U.S. suppliers and its Ohio factory workers for ideas to make the next Civic cheaper to build.

Shriver didn't yet know it, but back in Japan, Honda executives from President Nobuhiko Kawamoto on down had reached the same conclusion: The rising yen meant Honda could no longer afford to overengineer. So Hiroyuki Itoh, the Civic's chief engineer, began putting together his own team—one that within months would merge with Shriver's U.S. crew to collaborate on an all-out battle to wring costs out of the Civic.

**LOWER STANDARDS.** It would prove a difficult collaboration at times; for once, U.S. manufacturing engineers and marketers had a big say in shaping a new model from the earliest designs. With the high yen all but forcing Honda to boost local content from the U.S., the carmaker also worked far harder than ever before with North American suppliers. It even had to relax its vaunted

**ALL EARS:** Chief engineer Itoh, at wheel, got input from Shriver, second from left, and his team in Ohio

engineering standards. And Japanese engineers also used an unprecedented number of money-saving suggestions from factory workers and suppliers on both sides of the Pacific—often only after a struggle.

Now, Honda is about to find out if the hard work has paid off: With the unveiling of the new model in the first week of September, car buyers—and Honda's Detroit rivals—will get their first chance to see how well Itoh, Shriver, and team have done. The new Civic will provide a key test of Honda's—and the entire Japanese auto industry's—ability to remain competitive in the face of a strong yen and a muscular Detroit. For Japan's No. 3 auto maker, whose worldwide revenues hit \$46.9 billion for the fiscal year ended last March, the Civic's success is crucial. It's Honda's



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gest seller at home and abroad, accounting for a full third of the 1.78 million cars the company sold. In the crucial U.S. market, it's Honda's second-biggest seller, behind only the midsize Accord. "They can't afford to be a flop," says Alison Shimada, a Tokyo-based analyst with Fidelity Management & Research Inc.

**HOW COST?** Still, with the yen trading below 100 to the dollar, analysts believe Honda now loses money on every Civic it sells in the U.S. But Honda can't afford to swing the balance far from quality as it trims costs. Some critics say that Toyota Motor Corp.'s recent models have become too Spartan. Meanwhile, U.S. carmakers such as Ford Motor Co. have been criticized for improving features only by inflating excessive costs. "It's value we have to stress," Kawamoto says.

So how well has Honda succeeded? In Japan, the new 1996 Civics will sell for roughly 3.2% less than last year's models. In the U.S., new prices haven't

been announced: The 1996 Civics won't hit showrooms until October. But Honda is clearly trying to hold its line. "Our goal is to keep the same price range as the current model, even though the car is moving up in size and features quite substantially," says Thomas G. Elliot, executive vice-president of Honda's American sales unit. Analysts expect the cost of a new Civic to rise just above 1995 models; the popular four-door Civic LX, for example, should start at around \$16,600, roughly \$200 over last year. Although they won't reveal how much they've saved overall, Honda executives say that research and development spending and capital investments were flat what they were for the 1992 Civic redesign. Manufacturing costs have also been slashed. Analyst Christopher W. Dergren of AutoPacific Inc., a consulting firm in Santa Ana, Calif., estimates the new model costs some \$800 less per car to build than the old.

The 1996 Civic is an evolutionary step rather than a quantum leap from its predecessor. A fresh front-end design with sportier headlights gives a more European look, while the interior is bigger. The roof has been raised slightly and the rear seat has been pushed back, giving much-needed head- and legroom. In the U.S., a bigger, peppier 1.6-liter engine is now standard; one version will

## Honda Saved Enough Money Where Customers Wouldn't Notice . . .

- Replaced rear disk brakes with cheaper drums; switched to simpler, less expensive antilock system.
- Integrated dashboard clock into radio display.
- Replaced trunk hinge with a simpler design that cut costs in half.
- Used 30% fewer threads in rear seat materials and replaced vinyl and interior trim with cheaper fabrics.
- Bumpers, dashboard, and other parts are now made with fewer pieces, cutting manufacturing costs.
- Air conditioning that is factory-installed—rather than dealer-installed—trims price from \$1,200 or more to \$850.



'96 CIVIC: A high yen is a big burden

be the first mass-produced gasoline engine to meet California's tough new emission standards. And by fastening the engine onto the body with sophisticated hydraulic mounts and adding a new electronically controlled automatic transmission, Honda has given the Civic a much quieter, smoother ride.

Such improvements may not be enough to keep the Civic far ahead of the small-car pack, though. The redesigned 1996 Saturn is also quieter and more refined than its forerunner. Ford will replace its aging Escort with a more competitive version early next year. Honda may find it increasingly hard to convince buyers to pony up the typical \$2,000 premium over American rivals. "It's not head and shoulders above" competitors, says George C. Peterson, president of AutoPacific. "It's maybe just a head above."

The new Civic is the first Honda model entirely conceived and executed since Kawamoto shook up the company in the early 1990s. For 20 years, Honda's renowned R&D engineers had always dictated new designs. Success bred arrogance: Even in Japan, sales and manufacturing teams were only consulted after designs were nearly set; when disagreements arose, the engineers had the final word. And the U.S. unit had no say over any but cosmetic changes. "We always did

what we wanted, thinking it was the right thing," says Kawamoto, a 27-year R&D veteran who took over Honda's top job in 1990. "But we had to see that profits wouldn't keep growing." So, soon after the fifth-generation Civic debuted in 1992, Kawamoto ordered Itoh to begin by revamping Honda's design process itself. Because Honda's R&D specialists in the past hadn't sought input early enough from manufacturing, factories had rarely had time to test designs to minimize capital investment. Kawamoto also knew that Honda had to work earlier with suppliers to eke out production efficiencies.

## . . . To Add Features and Refinements Where They Would

- A more powerful 1.6 liter engine that meets California's tough new emissions standards.
- Hydraulic engine mounts and electronic controls for automatic transmission make for a quieter, smoother ride.
- Radio standard on all models; doubled number of speakers to four.
- Rear seat folds in two sections instead of one, adding versatility.
- A higher roof and improved design create a more spacious car with extra rear legroom.



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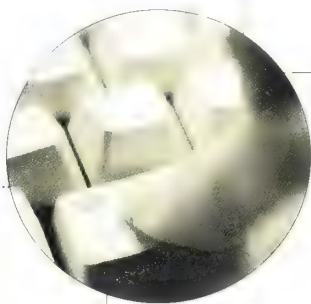
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WHERE DO YOU WANT TO GO TODAY?



Itoh formed his team, Shriver and a group of Ohio employees flew to Tokyo to outline their plans to ferret out excess costs in the U.S. "We received input from the factory much earlier," Itoh says. "We wanted to get sales thinking, 'How can we sell this?' and the factory thinking, 'How can we make this?'"

The result was a host of money-saving manufacturing tricks that Honda hopes customers won't notice. Although none brought huge savings individually, collectively they add up to a bundle. While the old Civic sported a complicated trunk hinge that made it easy to retrieve luggage, the new model returns to a simpler, traditional hinge that's cheaper to make, if not quite as convenient. Elsewhere, the dashboard and the inner door trim are made from one molded piece each, instead of two or more, which simplifies manufacture. And the cloth on the rear seats, which get less wear, has 30% fewer threads.

Still, Japanese designers and engineers sometimes accepted new ideas only after a struggle. For instance, East Liberty paint shop employee Jodie Kavanagh had a suggestion to simplify the design of front and rear plastic bumper covers, or fascias. On the old Civic, the front fascia had two separate air inlets and a bottom section that had to be individually masked before painting. In the summer of 1992, when Itoh and 10 Honda execs made a fact-finding trip to Ohio, Kavanagh proposed building the fascias with removable grills that wouldn't need masking. But the executives, cautious because Japanese consumers are very picky about paint, nixed the idea.

**SHOCKED ENGINEERS.** Unfazed, Kavanagh persisted. She countered with several alternatives, which executives presented at later design meetings. Eventually, Itoh accepted a compromise. The front fascia would have only one easily masked opening, while the rear would require no masking. Honda's annual savings: \$1.2 million in the U.S. alone. Honda's engineers "weren't accustomed to hearing from the factory so early on," says Kavanagh.

anagh. "They had to get over the shock."

The U.S. sales team also pitched in. The Civic's air conditioning and sound systems had always been dealer-installed options, for example. Dealers charged what they could get, typically \$1,200 to \$1,500. Now, however, air conditioning will be installed at the factory, for just \$850. Audio systems will see similar savings.

But by far the most straightforward way to chop cost was to boost the use of inexpensive U.S. parts. Although U.S. managers had long pushed for more local parts, Honda only slowly built relations with suppliers struggling to meet its tough standards. The rise of the yen changed all that.

Indeed, Honda eased some of its strict procurement rules to make it easier for innovative U.S. suppliers to win business. Shape Corp., a bumper suppli-

er that the best it could deliver was three millimeters. After much haggling, they split the difference. Says Itoh: "In the past, if a company's part didn't measure up we gave up, but this time we'd go back two, three, four times."

As a result, U.S. suppliers are providing 320 parts for the new car. Honda expects to buy \$1.93 billion in parts from U.S. suppliers next year for the Civic, a \$164 million increase from 1992. The 1996 Civic has 32 new American suppliers—for a total of 211—some of whom will also export to Japan. U.S. content has increased from 82% to 92%.

Back home, Honda was also working closely with suppliers to bring costs down. Nisshinbo Industries Inc., which had sold brake pads and linings to Honda for 30 years, was pressing it to also buy its antilock brake systems—already supplied to Mitsubishi, Nissan, and Sa-

zuki. In the past, Honda had designed its own antilock brakes, then had them manufactured by an affiliate. "We had studied the system and knew ours was better, but we were pitching hard," says a manager in Nisshinbo's American division. Honda pitched its own engineer against Nisshinbo as a competition to create

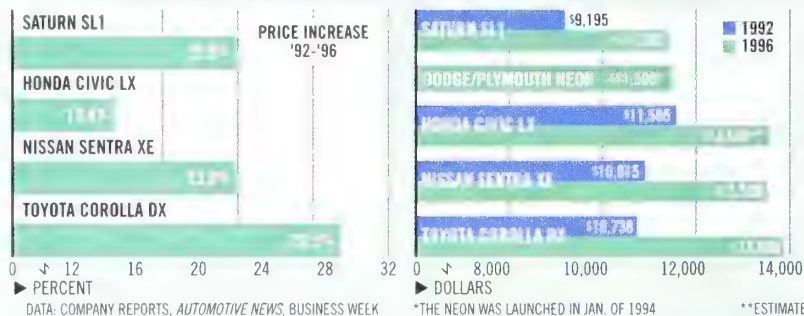
ate brakes for the Civic. In the winter of 1993, Honda engineers had to admit that the supplier's system, at half the weight and price, had all the performance. Nisshinbo won the contract.

So with Honda's factories around the world starting to spit out shiny new 1996 Civics, can Shriver and his colleagues finally relax and celebrate? They'd better not. Despite the dollar's recent recovery, many analysts expect the yen to continue its decades-long upward trek. And with Detroit steadily improving its small cars—while straining to maintain a \$2,000-per-car price advantage—Honda's entry-level sedan is under more competitive pressure than ever before. Time to get cracking on the Civic redesign for 2000.

*By Edith Hill Updike in Tokyo and David Woodruff in Detroit, with Larry Armstrong in Los Angeles*

## HONDA HOLDS DOWN CIVIC PRICES, BUT DETROIT MAINTAINS ITS EDGE

STICKER PRICE ON FOUR-DOOR SUBCOMPACTS WITH FIVE-SPEED MANUAL TRANSMISSIONS



er in Grand Haven, Mich., had no business with Japanese carmakers until 1993. That January, President Peter Sturuss and two associates carried several ski bags filled with bumpers to a Tokyo trade show. They expected to woo potential customers for five to eight years before landing a contract.

To Sturuss' delight, however, Shape signed a deal with Honda after just six months. Honda's engineers were won over because Sturuss' steel bumper had just three parts, vs. 13 for the prior version, cutting weight by two pounds and cost by one-third. Itoh and his team were so taken that they will use the bumpers not only in Ohio but on 36,000 Japan-made Civics each year as well.

Relations between the two companies hit potholes. Honda first insisted that Shape's bumpers be exact to within a millimeter of specs. Shape protest-

## A woman working in the East Liberty paint shop had an idea she wouldn't give up on. Annual savings: \$1.2 million



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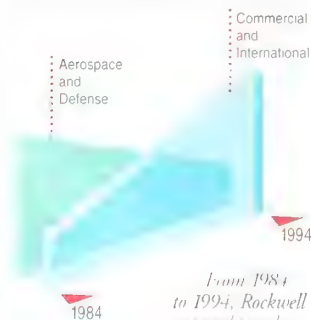


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# THE REVOLVING DOOR AT RUBBERMAID

Is CEO Schmitt's tough style driving executives away?

It's been a scorcher of a summer, and a particularly uncomfortable one for Rubbermaid Chief Executive Wolfgang R. Schmitt. On July 18, Schmitt announced that earnings at one of the most admired pillars of Corporate America plummeted by 49% in the second quarter, to \$29 million. Worse, the maker of those ubiquitous plastic housewares and toys predicts that its earnings could be flat this year because of soft household spending and increased resin prices. It's the first earnings setback since 1980 at Rubbermaid Inc., which has long been held up as a model of predictable growth, creative management, and rapid product innovation.

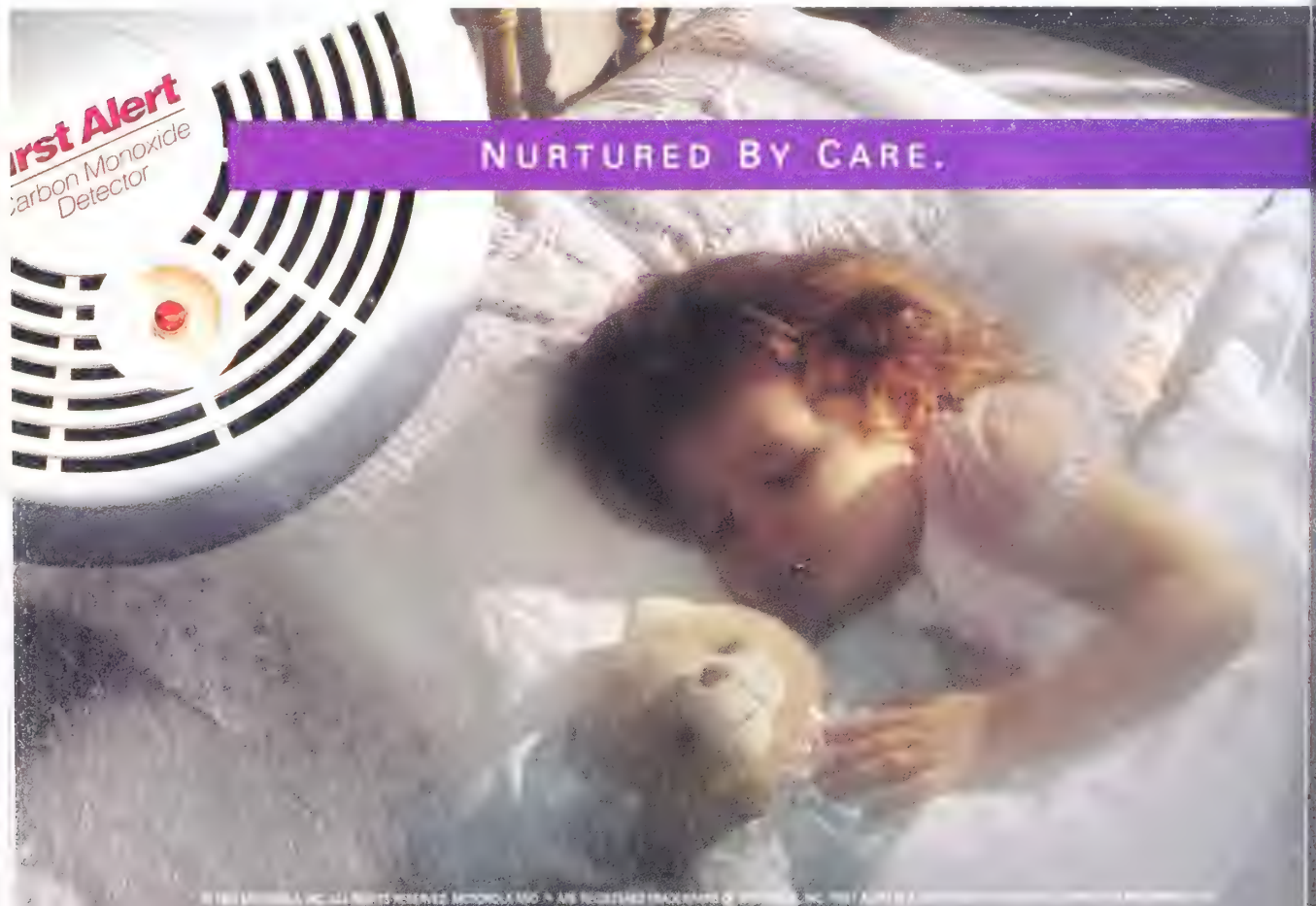
The problems at Rubbermaid go far deeper than cautious consumers and rising raw-material prices. The company, based in Wooster, Ohio, is racing to confront a raft of new competitors, while trying to placate its increasingly demanding retailers. Earlier this year, stores balked at Rubbermaid's attempt to raise prices to offset the doubling in resin costs, and Rubbermaid had to settle for less than it was asking.

**A WAVE.** At the same time that it's trying to cope with irritated clients, the company has been rocked by a wave of executive departures—many not voluntary—since Schmitt took over near the end of 1992 and began reshaping the

executive suite. Three division chiefs have left in the past 18 months. Two top managers of the company's international operation have departed in quick succession. And a slew of lower-level executives have also walked.

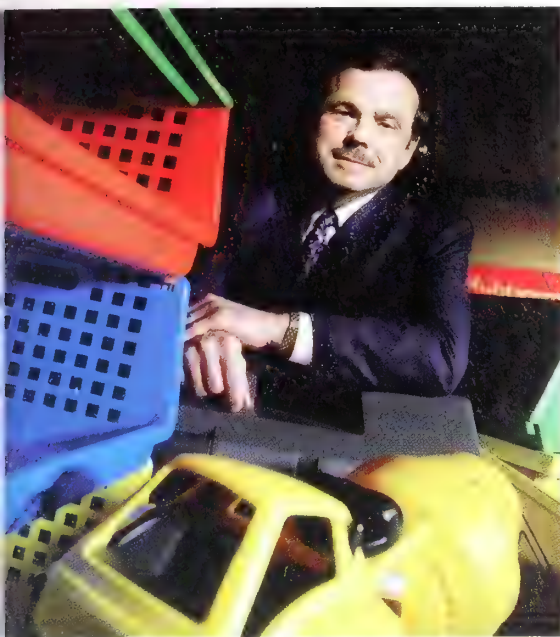
Former executives place some of the blame for Rubbermaid's turnover on the hard-driving, autocratic management style of Schmitt and his No. 2 executive, President Charles A. Carroll. "It's the Wolf and Chuck show, so division presidents who want to have independent thought don't last long," says John L. Mariotti, who ran the Office Products Division before leaving last year. Rumors at the company and on Wall Street are even buzzing that former CEO Stanley C. Gault, who retired in 1991 after a sensational 11-year run and remains on the board, will return. Although he provided plenty of guidance, Gault allowed managers greater freedom during his tenure, say those who worked with him.

Schmitt wasn't available to talk to *BUSINESS WEEK*. But Rubbermaid officials argue that the turnover isn't out of line, and that some managers the company has hired from outside haven't been comfortable with its fast-moving, team-based culture. As for the rumors



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"It's the Wolf and Chuck show, so division presidents who want to have independent thought don't last long," says a manager who left last year

SCHMITT SOMETIMES SAYS SUBORDINATES' IDEAS ARE "DUMB"

scrutiny it's been getting. It boasts some of the strongest of brand names and remains one of the consumer-products world's greatest innovators. It cranks out 400 new products a year, while making shrewd acquisitions to extend its product line. Perhaps one of its biggest successes:

Little Tikes, the maker of durable plastic toys, including the Cozy Coupe, which executives refer to as "the best-selling car in North America." Since Rubbermaid acquired Little Tikes in 1984, its sales have increased more than elevenfold, to \$500 million, according to Kemper Securities Inc.

Rubbermaid's financial fundamentals still look healthy, too. It has little debt.

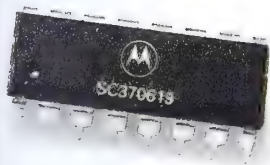
And until 1994, it usually hit its goal of 15% annual earning growth. Rubbermaid's profits are expected to rebound in the second half, thanks in large part to lower resin prices. Next year, analyst William H. Steele of Dean Witter estimates, earnings could climb 22%, to \$253 million, as Rubbermaid's sales hit \$2.6 billion, up 8%. "I don't think anyone is even beginning to count Rubbermaid down or out," says Tom Cordano, president of Tucker Housewares, a unit of Mobil Corp.

Still, in recent years the competition has started to close in. Little Tikes now faces strong challenges from Step 2, based in Streetsboro, Ohio, and Mattel's Fisher-Price. Both manufacture similar plastic toys. Even Rubbermaid's Con-Tact shelf liner is under pressure. Tiny Manco Inc., based in Westlake, Ohio, claims that it's gaining market

ut Gault's possible return, directors tacted by BUSINESS WEEK deny the orts and insist Schmitt has their support. He's "a very, very imssive executive," says director Paul Schloemer. Gault, who is retiring as of Goodyear Tire & Rubber Co. yearend, will not comment about bbermaid.

Rubbermaid isn't used to the harsh

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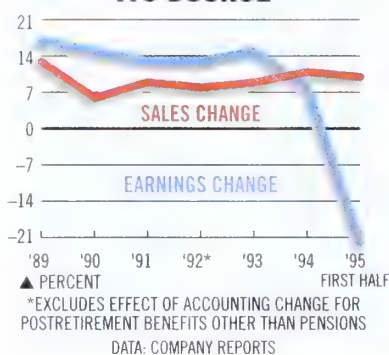
# The Corporation

share with its new nonadhesive liner.

Meanwhile, critics say the giant manufacturer hasn't done enough to please its retailers. Wal-Mart Stores Inc., which alone accounts for 15% of Rubbermaid's \$2.2 billion in sales, was especially annoyed at the company's efforts to hike prices, says a retail industry insider. The giant chain "punished them a fair amount" by reducing its marketing support for Rubbermaid merchandise, the source says. Rubbermaid wouldn't comment on how its pricing affected Wal-Mart but insists it has good relations with the retailer. For its part, Wal-Mart wouldn't comment about its dealings with Rubbermaid.

Rubbermaid's contretemps with Wal-Mart comes at a time when most other manufacturers are bending over backwards to please increasingly powerful retail chains. Rubbermaid has lagged in important areas, such as developing

## RUBBERMAID LOSES ITS BOUNCE



year's annual meeting, he outlined a variety of measures to cut costs and boost profits. These include centralizing administrative functions, such as accounts receivable, and standardizing computer systems among divisions. His goal: to chop \$335 million from annual costs within three years. So far, Rubbermaid says it's on track to meet its target.

New acquisitions have also helped Rubbermaid extend its product line and accelerate growth. One of the more promising is Carex Inc., which makes walkers and canes, giving Rubbermaid a

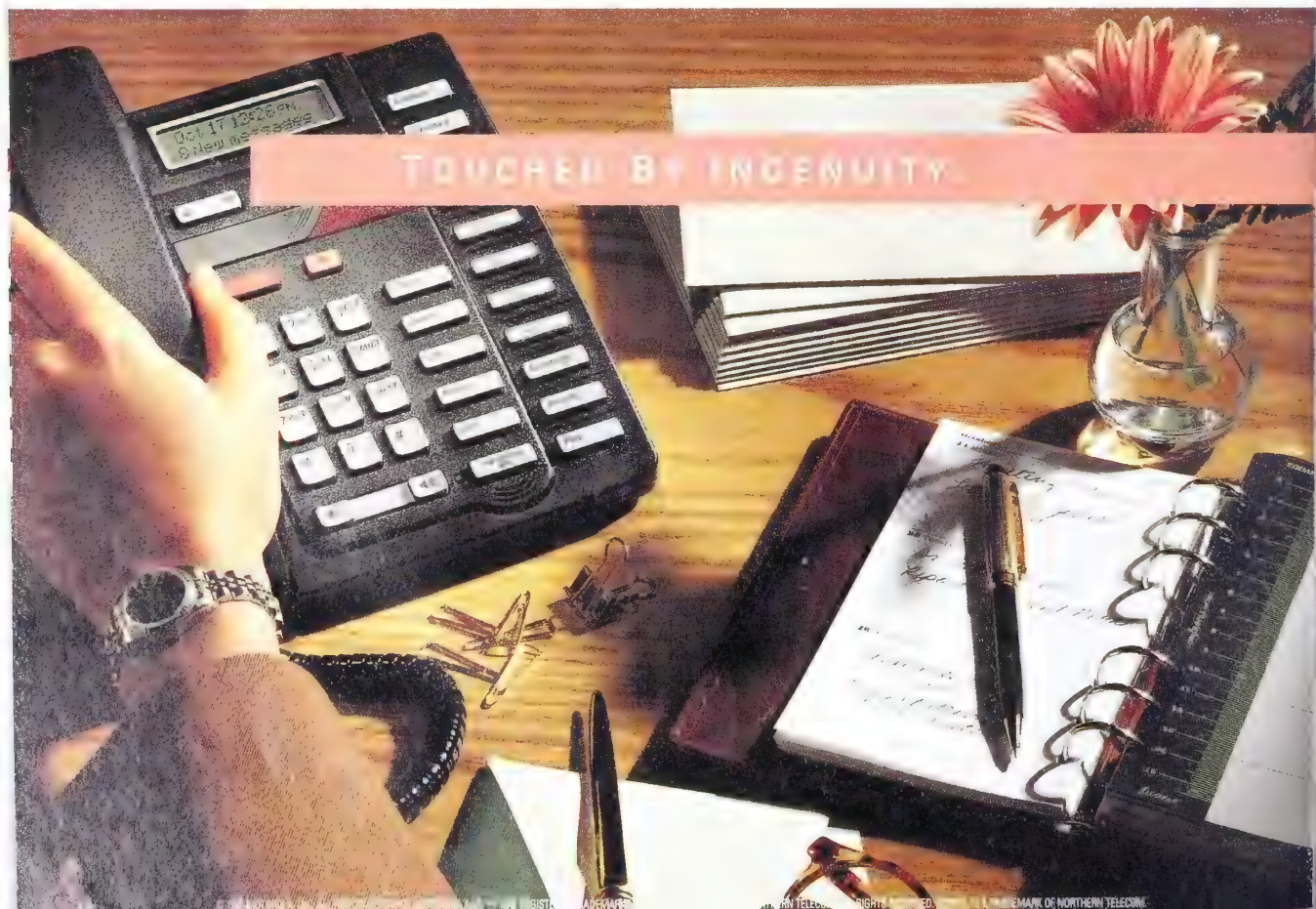
computer systems that automatically replenish retailer supplies based on actual sales, not forecasts. "They may have rested on their laurels too much," says one major retailer, who says Rubbermaid's systems for keeping its products in stock are less than stellar.

Schmitt has moved to address the new challenges. At last

toehold in the home health-care market. Altogether, the company's purchases have added about \$180 million yearly sales so far.

Rubbermaid is also upgrading computer systems to track inventory and improve service to retailers. Meanwhile, Carroll, Rubbermaid's president, has temporarily resumed his old job as head of housewares and is criss-crossing the country to repair damaged relations with customers.

**A CASUALTY.** Still, the upheaval in management may be impeding progress. Former executives say some of the recent turnover stems from Schmitt's tense, results-oriented style. The CEO, a 29-year Rubbermaid veteran, led the housewares unit for most of the 1980s, where he steadily improved performance. But Schmitt is not the most people-sensitive manager: He may publicly tell subordinates that their ideas are "dumb," says one ex-staffer. Numerous former managers also say he gets more personally involved than Gault in telling managers how to do their jobs. One recent casualty: Fred S. Grunewald, the company's housewares chief, who quit in May after only a year on the job. Rubbermaid says Grunewald shot





spent more time with customers gaining recent price increases. Newald won't comment. Rubbermaid's international staff has suffered many departures—at a time when the company is trying to expand its global presence. Schmitt has been counting on foreign markets to generate 30% of Rubbermaid's revenues by 1997, compared with 16% last year. Now, instead of relying on a centralized in-

ternational staff at headquarters to expand its market share abroad, Rubbermaid is leaving global growth up to its individual operating divisions. Its Little Tikes unit, for example, recently opened a new plant in Luxembourg and is expanding its distribution in Korea.

Still, Rubbermaid may not have the expertise to meet its international goals. Lately, the company has been hiring young MBAs with international backgrounds to try to create a multinational

culture, but the ranks of veteran international managers are thin. Schmitt was born in Germany and lived there until he was 10, but he has limited international experience.

That lack of global exposure hurts, say former executives. Last year, Rubbermaid pulled out of a joint venture with DSM, a Dutch conglomerate with a housewares unit. Rubbermaid was frustrated because it couldn't get a majority position. But Anthony Lenders, who ran the venture, claims the alliance

between DSM and Rubbermaid was uneasy because Schmitt refused to listen to DSM board members, even though he lacked overseas experience.

For now, investors seem willing to give Schmitt time to get the company back on track. While the stock has underperformed the market over the past four years, it has bounced back from recent earnings surprises. Still, it's currently trading at just under 30, little changed from the start of the year. Unless Schmitt can put Rubbermaid back on the corporate pedestal it once occupied and spark a livelier stock performance, he may find the winter months won't offer any relief.

*By Zachary Schiller in Cleveland*

## Rubbermaid's Strengths . . .

**PRODUCT DEVELOPMENT** Still among the best. Cranks out 400 new products a year.

**ACQUISITIONS** Joint ventures and smaller company purchases have expanded annual sales by \$80 million over the past year.

**COST-CUTTING** Well on its way to slashing annual costs by \$35 million by 1997. Reduced costs by \$60 million in the first half.

## . . . and Shortcomings

**PRICING** Because of more demanding retailers, unable to raise housewares prices as much as it wanted to offset recent increases in raw-materials costs.

**COMPETITION** Stronger rivals are chipping away at its share in key markets.

**MANAGEMENT** Turnover in executive ranks raises questions about company's ability to meet new challenges.

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## RETAILING

# I CAN GET IT FOR YOU RETAIL

Factory outlets are losing their price edge over regular stores



**R**enee Underwood recently took a day of her vacation to troll for bargains at two adjacent factory-outlet centers in San Marcos, Tex. But after six hours of wandering among the centers' 150 stores, the 38-year-old advertising executive left almost empty-handed. And one of the deals she thought she had snagged turned out not to be so great after all. Days after buying a \$12 pair of Lee jean shorts from the VF shop, Underwood found the same item on sale at her local Mervyn's for \$12.99—a better deal, she says, considering the 45-minute drive to the outlet centers. "I find if I shop smart at my local mall," says Underwood, "I can get better values."

Regional mall prices rivaling factory outlets? You bet: Malls are starved for traffic, and they're steadily narrowing the price gap. But that's just one of the challenges facing factory-outlet centers, which boast cut-rate prices on brand-name goods direct from manufacturers. Explosive growth in outlets is raising fears of market saturation. And outlet centers have been forced to get awfully spiffy to draw shoppers: Gone are warehouse-like buildings selling factory seconds. But the closer the outlet centers

**PLUSH LIFE:** The bare-bones barns of yore are no more  
get to regular malls in look and price, the less reason there is to shop there. "Factory outlets continue to bring in traffic, but the popularity they experienced in the 1980s is gone," says Wendy Liebmann, president of WSL Marketing, a New York consulting firm.

Factory-outlet malls have popped up across the country, usually 20 to 60 miles from a big city but often within reach of a vacation spot. Sales have more than doubled, to \$13 billion, since 1990 (chart). That kind of growth prompts some observers to wonder if the industry is overbuilt. "There are going to be too damn many of them soon," says Jack Shea, chief executive of Spiegel Inc., a catalog-sales outfit that also operates 17 outlet stores.

There are signs that this day may already have arrived. Although new centers have pushed total industry sales up, the take at stores that have been in place longer than a year is falling. For

the first seven months of this year, six comparable-store sales were down 2.6% from the same period a year ago. "I think there will be a shakeout," says Karen Goldberg, vice-president of the outlet-store division of Barneys New York. "Everyone's building them, but not all of them will be able to survive."

Investors have started to worry, says Jon Fosheim, a principal at investment adviser Green Street Advisors Inc. Outlet-center developers saw their stocks soar after they began going public in 1993—as real estate investment trusts. But so far this year, those returns were up just 0.4%.

**SWINGS AND SLIDES.** Outlet-center operators are fighting back with new brand-name tenants and different product categories, as well as such conveniences as food courts and playgrounds. Manufacturers make up the bulk of the more than 500 companies operating stores in outlet malls. But lately, such retailers as Ann Taylor, Barneys, Gap, and Saks Fifth Avenue have opened up alongside the manufacturers. Meanwhile, mall developers are bringing in new tenants from outside the traditional apparel base, such as IBM and Sony Corp. Baltimore developer Prime Retail Inc. is betting on athletics, with the introduction of Sports Court at some of its outlet malls, featuring clustered stores selling sports apparel, equipment, and footwear.

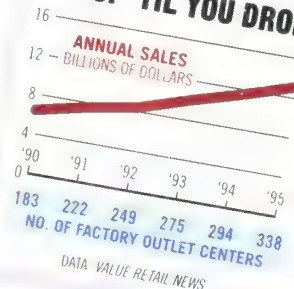
Analysts say new product categories should help. After 1993, apparel now accounts for 78% of outlet-mall shops, as clothing sales have been doggy industrywide. In 1994, outlets also are being squeezed by other retailers, particularly

department stores that have learned to compete by offering frequent, deep discounts on their own. They typically slice off as much as 30% to start with—and then drop prices even further. While most outlet centers promise savings of up to 70% off suggested

retail prices, consultant Alan G. Weinstein says that average discounts are about 25% to 30%. "The average shopper could probably do better if she waited for a department-store sale—and saved a lot of shoe leather and gas," he says.

Outlet-center executives argue they still have a major advantage. "You have

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## Marketing

to wait for a sale at department store for them to equal our prices," says William H. Carpenter Jr., president, Prime Retail. Still, outlet prices are higher than shoppers expect these days—mainly because more manufacturers are selling first-quality merchandise in their stores. The early days of the concept featured concrete, bare bones caverns with imperfect or excess merchandise, factory overruns, and last season's styles. Now, most outlet stores are well-designed boutiques arranged in fashionable shopping centers barely distinguishable from regional malls. In regular and damaged goods account for less than 15% of outlet merchandise, according to *Value Retail News*.

**WARY SHOPPERS.** So just what is an outlet store? That's a good question these days. Some, such as Toy Liquidators and Publishers Warehouse, are really just independent off-price retailers selling merchandise from many suppliers. Others are manufacturer-owned but sell goods designed exclusively for their outlets. Almost all of apparel maker Phillips-Van Heusen Corp.'s outlet goods are made specifically for those stores. Ann Taylor operates some of its 31 outlet stores under the name Ann Taylor Loft. Those stores feature a "bridge line" manufactured specifically for them. "Ann Taylor created this line for people who like the Ann Taylor look but can't afford it," says J. P. Morgan Securities Inc. analyst Lee Schalop. But some wonder if such shoppers will be satisfied with the cheaper line. "The jury's still out on whether this will work," says Schalop.

New formats and shrinking discounts have left customers suspicious of factory outlets and their supposed bargains. "There is some confusion as to what we really are and what we represent," concedes Jeffrey Kerr, president of Developers of Outlet Centers (DOC), a trade group. DOC plans to roll out a nationwide public-relations campaign this winter to help educate shoppers.

Of course, lots of outlet shoppers leave happy. Take Dorothy Lofton, a marketing executive at a San Antonio software maker. She plunked down nearly \$500 during a recent spree at the San Marcos outlet centers, loading up on shirts, sweaters, and slacks. Lofton figures such a haul at a department store would have cost twice that. "I do a lot of shopping. I know a good bargain when I see it," she says. Maybe. But plenty of bargain hunters find they no longer have to trek to a distant outlet mall to bag the big savings.

*By Stephanie Anderson Forest  
San Marcos, Tex., with bureau reporter*

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## Legal Affairs

### PENSIONS

# CAN A COMPANY HOLD A 401(k) HOSTAGE?

A Southwest Airlines case has alarms ringing

**A**t first blush, Gloria J. Cruz's beef with Southwest Airlines Co. seems like a typical employment dispute. After alleged problems with a new boss, Cruz charged the company with age and sex discrimination in a filing last year with the Equal Employment Opportunity Commission. A month later, four years after joining the company, Cruz was fired for what Southwest claims was a bad attitude and poor performance.

But Cruz's complaint is hardly garden variety. That's because she bumped into a little-known, unwritten policy followed by Southwest in managing its 401(k) retirement and profit-sharing plans. When the former Houston-based cargo manager went to collect some \$19,000 in 401(k) and profit-sharing money after her firing, Cruz discovered that Southwest would not release the funds—at least not until she signed a waiver promising she wouldn't try to get her old job back. Southwest, a company that calls itself "the love airline" and is widely praised

for its employee-friendly ways, won't disburse 401(k) or profit-sharing funds to ex-workers as long as their efforts to seek reinstatement are unresolved.

**"VINDICTIVE."** Unemployed and caring for a husband with Alzheimer's disease, Cruz, 55, says she had little choice. Last February, she signed the waiver and took a 20% tax hit, including penalties, for withdrawing her retirement money early. "They [Southwest] were tightening the screws," says Cruz, who, despite the waiver, is pursuing reinstatement and damages in a discrimination lawsuit set to be tried in Houston early next year.

Says Cruz's attorney, Bruce A. Coane, "She was forced to sign this thing to get what was rightfully hers." Adds Dennis R. Coleman, a benefits consultant with Kwasha Lipton: "It seems that, at most on its face, it's being vindictive."

Cruz's case and Southwest's 15-year-old policy are raising concerns about how much power companies can wield over the 401(k) plans that employees increasingly rely on to fund their retirements. Companies routinely ask peo-



**CRUZ:** Fired, she had to agree not to fight it to get her cash

sonnel to sign waivers in exchange for benefits such as fat severance packages. But Southwest's practice seems to go one step further: It uses an employee's own money as leverage against the employee. Though some benefits consultants question the policy, they say that if a company as successful as Southwest can get away with it, others may want to copy it—a prospect that alarms some EEOC officials. "We believe that that type of practice is discriminatory," says Jerome N. Scanlan, an EEOC attorney.

Southwest defends its policy as





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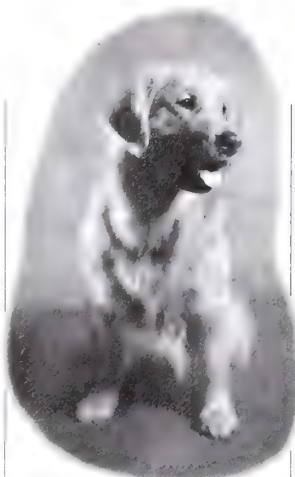


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## Legal Affairs

sound business practice that actually protects employees as well. The Dallas based carrier argues that if terminated employees could get their hands on their retirement funds early and then get reinstated in their jobs, the IRS might take the disastrous step of withdrawing preferential tax treatment of the company's entire 401(k) plan. (The IRS has never ruled on this issue.) Southwest also fears that, in this scenario, some employees might get a windfall not available to others. "We think this is a fair policy, which is uniformly applied," says Southwest General Counsel James F. Parker, conceding that the tax issue is not "clear-cut."

**REASONABLE?** Although many tax experts—and company executives—are leery of Southwest's argument, the airline has some legal ammunition on its side. In a 1988 challenge to the airline's policy by two former employees, a federal court in Dallas concluded that Southwest had not violated the Employee Retirement Income Security Act governing benefits plans because it applied its policy uniformly. It also found that Southwest, which in that case cited administrative burdens, not the tax-exemption issue, had "reasonable bases" for its practice from a business standpoint.

A similar suit brought in 1987 by the EEOC against family-owned manufacturing outfit J. M. Huber Corp. in Edison, N.J., ended the same way in 1993. The agency had charged Huber with illegally withholding retirement funds from ex-employees who had filed discrimination complaints. But a district court concluded that the practice had a "significant relation to a legitimate business concern." Still, Huber changed its rule and now pays retirement funds without delay to any fired workers, says spokesman. Both rulings seem in keeping with judges' aversion to overriding retirement-plan administrator's authority. Says Mary Kathryn Kelly, an expert in employee-benefits law: "Courts are very reluctant to get involved in cases which challenge the decisions of the fiduciaries of these pension plans."

Even so, many companies, including Hewlett-Packard, General Electric, and Tenneco, have steered clear of Southwest's practice. "Our view is that it's their [the employees'] money," says an IBM official. Since so few courts have addressed the issue, the conduct of such companies as Southwest could still be challenged. But Coane, Cruz's attorney, advises employees to sidestep the problem altogether: Get your money first. Sue later.

*By Wendy Zellner in Houston*

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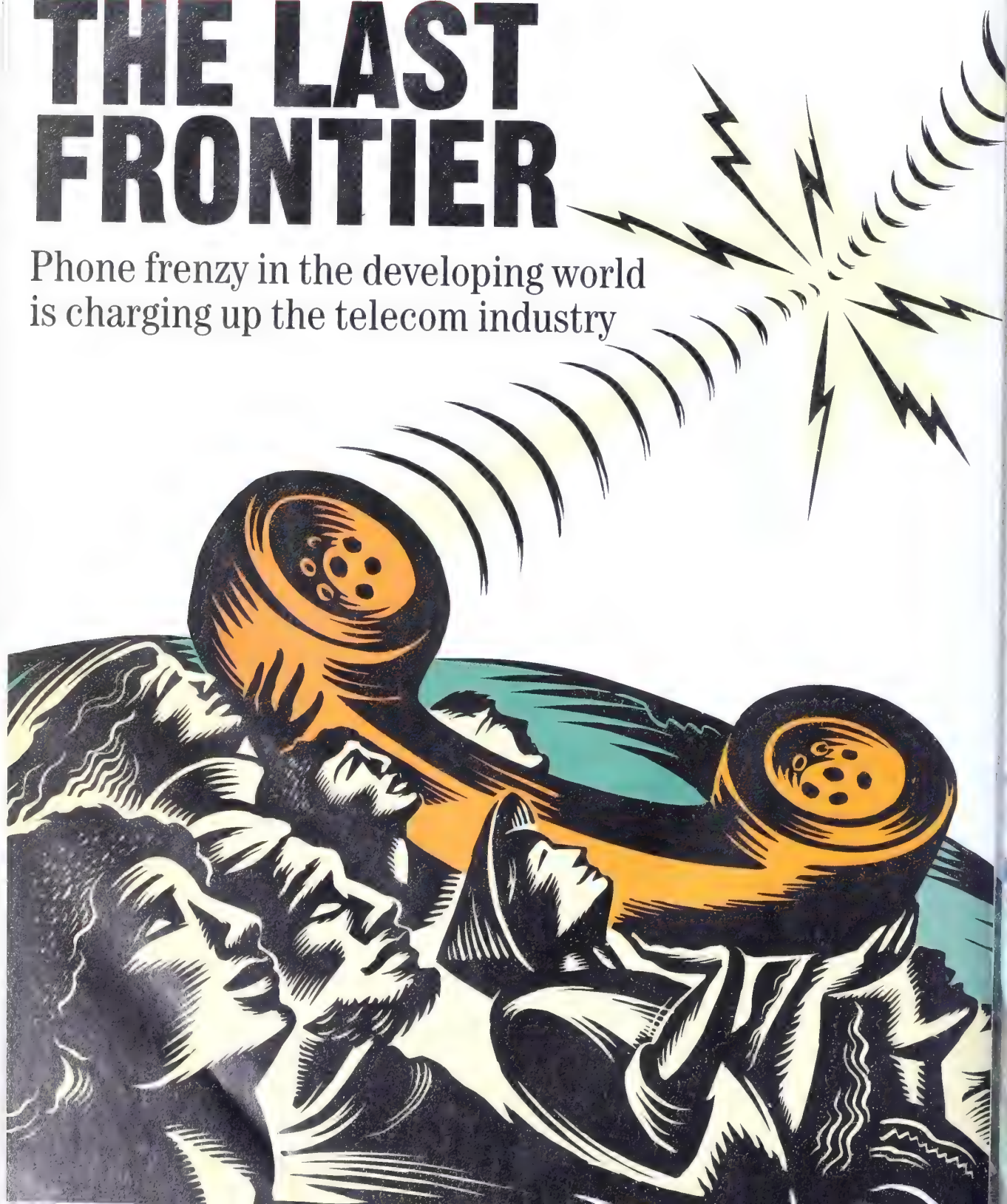
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Special Report

# THE LAST FRONTIER

Phone frenzy in the developing world is charging up the telecom industry







## Emerging nations plan to hike the number of phone lines by 11.7% a year for the next five years—vs. 3.7% for rich countries

**C**hile may be the most happening telecom market in the world right now. Last November, in an effort to jump-start its woefully inadequate phone system, the government threw long-distance and international calling markets open to competition and eliminated rate regulations. The number of carriers serving Chile's 14 million people shot from two to nine, and demand skyrocketed. Chileans made 10.2 million minutes' worth of long-distance calls between January and July, twice as many as in the same period a year before. International calling minutes soared 77% in 1994's fourth quarter. Calling revenues are rising at an annual rate of 14%, twice as fast as the overall economy.

Problem is, nobody's making much money. The free-for-all ushered international calling charges as low as a penny a minute in December—Chileans were calling China just to find out what Chinese sounded like. In the first quarter of this year, Chile's phone companies were among the handful in the world that didn't turn a profit. It doesn't help that their billing systems are primitive: In December, one woman was billed just \$18 for seven hours of calls to the U.S., Malaysia, Israel, England, Sweden, and Australia. In July, one 22-minute call to Canada cost her \$180. Telex Chile's hand-delivered bills arrive long after payment is due. Entel, the former long-distance monopoly, sent customers four sets of monthly bills in five weeks.

So who would want to do business in Chile? How about BellSouth, Bell Atlantic, SBC Communications, Italy's STET, Telefónica de España, and Samsung Group? They're already in, and Sprint and MCI Communications may decide to join the fun. BellSouth, which saw its share of the Chilean long-distance market double from January to July, to 7%, plans to invest up to \$300 million in the country by the year 2000. We knew it would be difficult coming in, and this has been

confirmed," says Gerald Breed, general manager of Bell South Chile.

That's life in the lands that the Information Revolution forgot. From South America to Africa, Asia, and Eastern Europe, less-developed and emerging economies around the world are the last frontiers for the telecommunications industry. As Chile's wild ride shows, the road to a wide-ranging, modern telecom system is seldom smooth. What with changing political regimes, collapsing currencies, widespread corruption, union opposition, and unpredictable surges in nationalism, any foreign company doing business in an emerging nation must be prepared to hang in there for the long haul. After all, it can't just rip out its lines and go home when times are hard.

But the near-term hassles and risks pale beside the potential gains: The world's developing countries have laid out plans to spend on the order of \$200 billion in the next five years to bring their phone networks—and nations—into the 21st century.

**PRIMING THE PUMP.** Granted, planning and actually spending are two different animals. And it might seem a lot easier for the world's biggest telecom companies to stay home. Deregulation and new technologies are making telecommunications hot in the U.S. and Europe, too. But those regions are moving toward liberalization in fits and starts. And even if Congress agrees on a telephone deregulation bill and nations such as France and Germany open up their markets, there won't be the same potential for growth.

No, for the biggest returns, it pays to look to the developing world. Right now, a handful of high-income countries, with only 15% of the world's population, lay claim to 71% of the world's main phone lines—the ones that connect the subscriber to the central switching office (map, page 100). More than 50% of the world's people have never even used a phone. So dire is the situation that the International Telecommunication Union (ITU) defines universal service as when everyone in a country lives within five kilometers of a phone. Forget about a handset in every kitchen.

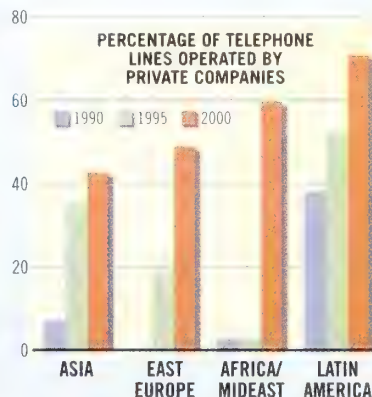
That kind of scarcity makes the telecommunications busi-

## Calling For Investment Telephone company privatizations in developing countries

| 1993        | 1994     | 1995           | 1996       | 1997        |
|-------------|----------|----------------|------------|-------------|
| Latvia      | Hungary  | Bolivia        | Albania    | El Salvador |
| South Korea | Pakistan | Cape Verde     | Ghana      | Honduras    |
| Singapore   | Peru     | Cote d'Ivoire  | Guinea     | Poland      |
|             | Russia*  | Czech Republic | Moldova    |             |
|             |          | India          | New Guinea |             |
|             |          | Indonesia      | Nicaragua  |             |
|             |          | Sri Lanka      | Panama     |             |
|             |          | Thailand       | Paraguay   |             |
|             |          | Turkey         | Russia**   |             |
|             |          | Uganda         | Taiwan     |             |
|             |          |                | Zambia     |             |

\*Russia's 86 long-distance companies

\*\*Sale of Rostelecom, Russia's long-distance and international carrier



DATA: PYRAMID RESEARCH INC.



# Telephone Haves and Have-Nots

More than two-thirds of households around the world have no telephone service. It's easy to figure out where they are: The least and lesser developed countries account for more than 77% of the world's population but only 5% of the world's phone lines. Cambodia is the worst off of all, with only 0.06 phone lines per 100 inhabitants. The U.S. has close to 60. There are some 47 other countries with less than 1 phone line per 100 people.

DATA: INTERNATIONAL TELECOMMUNICATION UNION



ness as sure a thing as death and taxes. Despite a widespread recession, constant demand for more phones caused the annual growth in main lines around the world to steadily accelerate for the past decade from 4.5% to 5.2%. The future looks even brighter, according to the ITU: The world's countries want to spend some \$60 billion per year through 2000 to build 310 million main lines—two-thirds of which are targeted for developing nations. These countries, home to 80% of the

world's population, plan to increase the number of phone lines by an average 11.7%

a year for the next five years, compared with 3.7% for the world's 24 highest-income countries.

China alone is a huge market and challenge for equipment makers. The world's most populous nation wants to install 100 million digital lines by the end of the decade, at a cost of \$40 billion. Its goal: Elevate telecom penetration from 3 lines per 100 people to 8 in five years. That means it will have to install a network the size of Bell Canada each and every year. "China is the hottest opportunity in the world," says James R. Long, president of world trade for Canada's Northern Telecom. "Everybody is trying to get in there."

Whether it's in China or

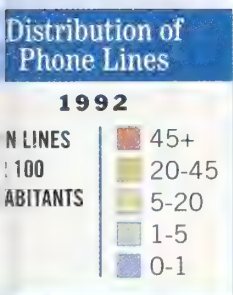
Chile, there's good reason for this phone frenzy. Emerging nations realize they cannot develop their own economies or hope to compete in world markets without top-notch communications systems. For proof, all they need do is plot their gross domestic product and the number of phone lines per capita on a graph. There is a one-to-one link: The higher the number of lines, the higher the income. With the global economy shifting more toward services, countries that aren't adequately wired will fall further behind—especially if they want to be more than the sweatshops for the world and attract high-tech, high-salary businesses. As one U.S. government official says: "If you are not connected to the global network, you are nowhere."

In nation after nation, a modern communications infrastructure is priming the economic pump. Take a look at Turkey. It started upgrading its network in the 1980s, pushing the number of phone lines per 100 people from 3.5 in 1983 to 16 by 1992. Today, Turkey's calling revenues are high enough

to pay for development of the network itself, eliminating the need for foreign loans to prop up the phone system. A domestic telecom-equipment manufacturing sector has also emerged, exporting switches. In the same period, Turkey's GDP per capita rose to \$1,905 from \$1,460.

Still, poor nations can't start their network upgrades

**China plans to spend more than \$40 billion, installing the equivalent of a Bell Canada-size network each year until 2000**



without massive infusions of foreign investment, skills, and technologies. To get them, countries are loosening regulations and opening their doors to foreign telecom companies of all types. Equipment makers flood through first—AT&T, Motorola, and Northern Telecom from North America; Alcatel Alsthom and Siemens from Europe; NEC from Japan. The developing nations may lack capital and technical savvy, but they do have a future source of cash—a steadily rising stream of calling revenue once the gear is in place.

In a typical deal, the foreign equipment maker or phone company funds the network and maybe even runs it—getting a guaranteed stake in future revenues. Foreign telecoms are swamped with opportunities in the developing world to buy equity stakes in phone companies, snap up cellular licenses, or build and operate a network for a number of years before transferring it back to the country. “There are many, many development projects where we as a manufacturer must take a share in the risk of providing and installing equipment to developing nations,” says Bert de Grave, director of op-

erations for Alcatel Alsthom’s international division.

For the really big projects—building 3 million lines in Argentina, for example—countries are willing to sell off the phone company to a foreign operator. But there are lots of variations for smaller deals: Soft loans, joint ventures, build-operate-transfer agreements—all are becoming commonplace for equipment makers who elsewhere simply install the equipment and move on.

Motorola Inc., for example, is best known as the top supplier of cellular-phone equipment. But it set up a unit in 1988 to operate systems in the developing world through joint ventures with local partners. It now runs 20 networks. “At the start, we saw it as a good way to kick-start equipment sales,” says Michael Norris, head of Motorola’s joint-venture business. “But it’s been a very good revenue stream.”

**PRETTY PAYOFFS.** Where are the opportunities? Start with the list of nations that are set to sell off their state-owned phone companies. There are 26 phone-company privatizations scheduled for the next three years in emerging markets (time line). At the same time, licenses for new wireless networks are being issued at a head-spinning pace. India, for example, is auctioning off 40 cellular licenses—two for each of 20 operating regions.

Where markets open, capital quickly follows. “In Europe, they are liberalizing in order to introduce competition. In the developing world, they are doing it to raise cash for the network,” says William W. Ambrose, president of Pyramid Research Inc., a telecommunications consultancy in Cambridge, Mass., that specializes in developing nations.

The money won’t flow, however, if the local governments can’t be trusted. Right now, investors are wary about bidding in India’s cellular auctions because the government abruptly canceled a \$2.8 billion contract with Enron Corp. to build a power plant, even though construction had already started. If one deal is shaky, though, the money will quickly flow to the better ones. “There is a substantial amount of capital in search of investment opportunity,” says Michael T. Masin, president of GTE’s international business.

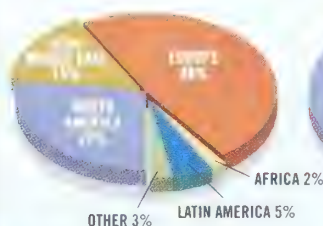
For the companies that choose wisely, there are big returns. Northern Telecom’s annual sales in the Asia/Pacific region have tripled in the past three years, to \$1 billion. U.S. West Inc.’s \$100 million investment in a Russian phone company in 1991 has also risen threefold in value. Nynex Corp. bought a 15% stake in a newly formed Thai phone company, TelecomAsia, for \$470 million in 1992. At the time, analysts complained that Nynex was overpaying. Today, its stake is valued at \$1.2 billion (page 102).

Those kinds of payoffs have filled the air routes to Asia, Latin America, and Eastern Europe with telecom executives from companies large and small. “You can’t be a player in this business if you’re not in the developing coun-

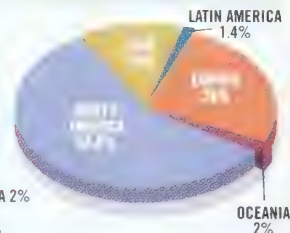


## Opportunity Calling

SHARE OF OUTGOING TRAFFIC, IN MINUTES  
1992 TOTAL=41 BILLION



CELLULAR SUBSCRIBERS BY REGION  
1992 TOTAL=23 MILLION



DATA: INTERNATIONAL TELECOMMUNICATION UNION



tries," says Martin Shum, chief executive of ACT Networks Inc., a California-based manufacturer of equipment that increases satellite network capacity. "That's where all the growth is. That's where all your competitors are."

But doing business in developing regions requires a leap of faith that the conservative

## Special Report

phone companies of the industrialized world have rarely needed to make. And the risks are as much political as financial. A developing country's state-owned phone company does

a lot more than transmit calls. It is often a nation's large employer. Phone tariffs can subsidize everything from school to the presidential palace. And international calling revenues—boosted by huge surcharges—are a primary source of hard currency for poor nations with few exports. "Telecom is an intensely political business, and not just because of the size of the investment," says Ken Zita, a consultant with Network Dynamics Inc., a New York-based telecom adviser developing nations: "There are so many really fundamental macroeconomic and political issues involved."

In some cases, politics have sandbagged ambitious teleco

# NYNEX' EXCELLENT ADVENTURE IN THAILAND

**W**hen companies invest in the developing world, conventional wisdom holds that they should avoid political strife. But sometimes, the conventional wisdom is plain wrong. So says Nynex Corp., which was in the midst of negotiating a 15% stake in a joint venture to build 2 million main phone lines in Thailand when a coup broke out. Violent street clashes in April, 1992, between pro-democracy civilians and the military, forced King Bhumibol Adulyadej to rebuke the government.

"We were just reaching the final stages of negotiations, and a lot of companies were leaving the country," says Nynex Vice-Chairman Frederic V. Salerno. But executives of the Charoen Pokphand Group (CP) of Thailand, the majority partner in the venture, pointed out to the nervous New

Yorkers that their country had weathered several coups in the past two decades, and economic growth continued unabated each time. "We figured that since coups never made a difference, we weren't going to bail out," Salerno says.

**WELL-HEELED.** Smart move. Today, Thailand has a democratic government, and Nynex' \$470 million investment in Thailand is worth \$1.2 billion. Its partnership with CP, TelecomAsia, went public a year after it was formed and has a market capitalization of \$8 billion, making it one of the best-heeled carriers in Asia.

Nynex' Thailand adventure is a case study in how to do things right

in a developing country. The Baby Bell, looking for opportunities outside its highly regulated New York and New England calling regions, started by picking a country that met its international investment criteria—strong economic growth and a driving need for telephone infrastructure. In 1992, Thailand's gross domestic product was growing by 10% a year, but it had only 3 phone lines per 100



**BANGKOK TEST:** Nynex' \$470 million investment is worth \$1.2 billion

people. The government wants 10 per 100 by the turn of the century. It awarded a license to TelecomAsia to build 2 million lines, operate them for 25 years, and then transfer the whole thing back to the government.

CP, an industrial conglomerate with no telecom experience, needed a partner that could handle a project that size. It had been negotiating with British Telecommunications PLC, but BT refused to take an equity stake. Nynex was chosen, a CP official says, in part because of its presence in the world's most complex phone market. Once you've run New York's network, their thinking went, Bangkok would be a piece of cake.

Then came the hardest part: doing the deal. "The subtleties were in the translations," says Salerno. "The lawyers always seemed to be writing up something different than what we had said." So Nynex and CP had the lawyers write each point down as they agreed to it, so that there wouldn't be any confusion later.

For Nynex, its biggest negotiating point was to maintain operating control, despite its minority share. "We never blinked on that," says Salerno. It also won a fight with CP over the right to appoint the chief operating officer. "We told them that the reason we're here is because you want our expertise, so let us use it," he says.

CP has no regrets. It's ahead of schedule on the buildup, and TelecomAsia recently won the license to build Thailand's first cable-TV network.

But CP is most pleased with the relationship it has built with Nynex executives. "All along, Nynex has sent us their best people," says CP President Sunthorn Arunanondchai, on a recent trip to New York. "When we come here, they take us into their homes. Even though it is a 30-hour flight to Bangkok, Mr. Salerno always comes to our meetings." That kind of personal attention has paid off for Nynex. CP has taken it as a partner in China, where the Thai group is already well established. "We consider ourselves bound at the hip," says Salerno. "The Thais have become like our family."

*By Catherine Arnst in New York*

# Exploring the limitless potential of multimedia.

*Today, multimedia has changed the way we perceive education, and indeed, the world. A simple computer screen has become a landscape to explore, a window to another world. For a student, all it takes is a keystroke or the click of a mouse to access the universe. This rapid development of information and communications technology has created new ways of living, relating and educating.*

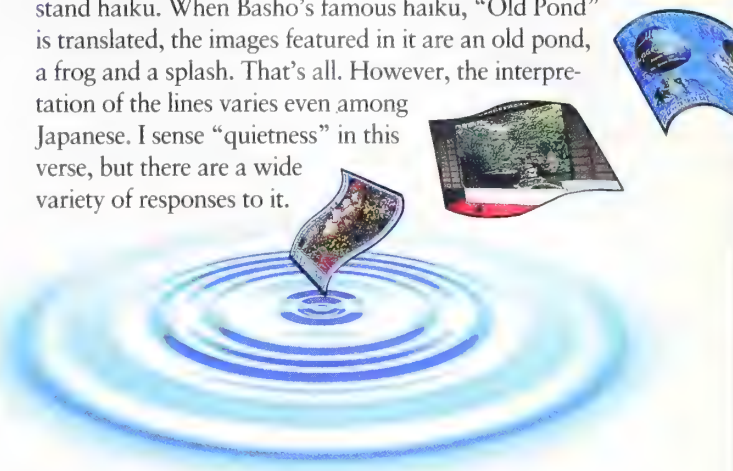
*Recently, in the upper reaches of the NEC Supertower in Tokyo, two experienced communicators shared their impressions of the coming multimedia age, education and even haiku. John Nathan holds the Takashima Chair in Japanese Cultural Studies at the University of California, Santa Barbara, and has been translating Japanese literature, and writing and directing films for more than 30 years. His translations include the early novels of Nobel Prize winner Kenzaburo Oe. Tadahiro Sekimoto earned a Ph.D. in Engineering from Tokyo University. His steady rise through the NEC ranks placed him as chairman of the board in 1994. He has also served as vice chairman of Keidanren, Japan's Federation of Economic Organizations.*

*Here's a taste of what Professor Nathan and Dr. Sekimoto had to say about the merits of education and information in the multimedia age.*

**Professor John Nathan:** A few days ago, I visited Kenzaburo Oe, who has been a close friend for 30 years. Whenever we meet, we always play a game together. He reads me his Japanese translation of an original English poem, and I put his translation into English. Then he shows me the original English verse for the first time, and we compare it with my English

translation. The versions are often worlds apart. What's interesting, is that the essence of information is really difficult to communicate.

**Dr. Tadahiro Sekimoto:** I agree with you. For example, I think for many it is most difficult to understand haiku. When Basho's famous haiku, "Old Pond" is translated, the images featured in it are an old pond, a frog and a splash. That's all. However, the interpretation of the lines varies even among Japanese. I sense "quietness" in this verse, but there are a wide variety of responses to it.



**Nathan:** Let's go more deeply into this idea. When we try to grasp information only in terms of an array of facts, there is a great deal that cannot be conveyed. Unless we take into consideration the values, world views and sensibilities that are peculiar to an individual culture, we are merely exchanging facts. For example, there is no explicit reference to "quietness" in the Basho haiku, yet as a Japanese, you are sensitive to the cultural assumptions underlying the language.

**Sekimoto:** Exactly. So, if there are some images and sounds that can communicate this scene—a splash and spreading ripples—I think people could understand the verse more clearly and vividly. Multimedia becomes a method of expressing a writer's intentions, a means of translating culture.

**Nathan:** Well you've mentioned "multimedia." A very hot term these days. But what exactly does it mean to us?

# "Any place on earth can become a classroom."



**"I believe multimedia will provide us with the potential for enhancing our minds and our lives."**

**Sekimoto:** My definition of multimedia is twofold. First,

multimedia makes possible the management of a variety of information—not just text, sound or image alone,

but all together in a true media mix. This I call "multi-information."

Second, it can be called "multi-transmission."

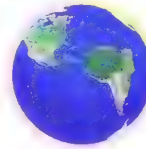
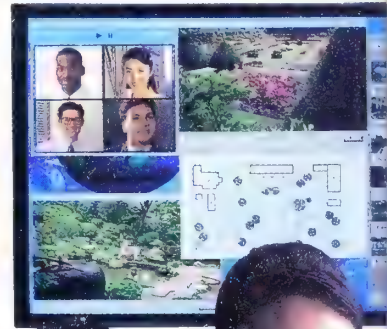
Means of transmission are many and varied, such as satellites and fiber optic systems.

Through these products we are delivering and receiving more diverse and more complex information—both sounds and images at the same time. By taking advantage of the scope of possibilities multimedia offers in both quality and quantity, I believe we can give education a new dimension.

**Nathan:** By exposing a limited number of students in my actual classroom to sounds and images, I can create, or at least imitate the highly effective learning environment that multimedia makes possible.

But what of all the would-be learners around the world who are unable to attend class?

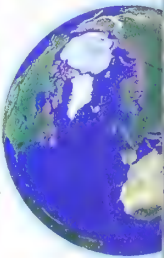
**Sekimoto:** That's an important point. Unlike the traditional educational format of an instructor speaking to a limited number of students in a classroom, the same lecture could be available to people on the other side of the globe.



MULTI  
CULTURAL

POTENTIAL  
imagination

Through multi-transmission, any place on earth can become a classroom. Some call this "distance learning." And it can pertain to all kinds of schooling, including continuing education and job training. NEC would like to illustrate some of these applications in Global College.



# Global

*Dr. Tadahiyo Sekimoto*



EC's Global College is an international community of students and educators linked through computers, and using multimedia communications tools to absorb knowledge, discover new worlds and experience different cultures.



**Nathan:** Speaking of Global College, I saw an excellent example of learning through multimedia. In an interactive computer game, set in 13th century France, features courtship rituals in the feudal age. Students play the role of a peer who is going to select a bride. In the game, they must get into another's skin, into the feel of decision-making based on the clues of another century. I call this simulation, or pseudo-experience.

**Sekimoto:** That's the beauty of multimedia, it allows you to experience something with all your senses as if it were real, such as in virtual reality applications. The student interacts with the computer, and thus interacts with the information. Moreover, as people's needs become more and more specific to their own lives, interactivity becomes an indispensable element in tailoring education to the needs of the individual.

**Nathan:** Precisely. To me, the excitement of NEC's Global College is that it will allow an educator to establish contact with anyone who has access to a terminal, and to provide that student with a full range of cultural data—music, interviews, even the ancient pond you mentioned earlier. With the student virtually swimming in a sea of input, the teacher becomes a guide to vivid new experiences and discoveries. This scenario strikes me as an ideal mode of education.

**Sekimoto:** What you just said outlines the characteristics of multimedia. While the students may be really "swimming in a sea of input," the state of

multimedia today is merely a stream and there's no telling how wide it will become. I believe it will eventually become a roaring tributary of potential as we enter the 21st century.

Take, for example, NEC's corporate slogan, "C&C for human potential." We have always considered "C&C"—the integration of computers and communications—a means to enhance human potential. Looking back on it now, I'm sure that the C&C concept was really the source for our multimedia aspirations. Through C&C, we have developed a wide range of hardware and software products with multimedia in mind. From the tiniest micro technologies to our largest industrial applications, NEC is providing the means to enhance human potential. But, above all, I think a central concern should be the sense of richness people feel in their lives. There is material richness and richness of mind. I believe multimedia will provide us with the potential for enhancing our minds and our lives.



*Prof. John Nathan*

# College



**"Connect!"** At TELECOM 95, John Nathan and Howard Rheingold will demonstrate NEC's Global College. Yet another example of the technology that we hope will become the vanguard of education in the future.

For further information contact: NEC Corporation, Overseas Advertising Division, 7-1, Shiba 5-chome, Minato-ku, Tokyo 108-01 Japan.



# NEC



upgrade plans. Take Kenya, where the World Bank tied a telecom loan to deregulation. The national phone company would have had to eliminate thousands of jobs to become more efficient. "They tried to get the funding and pretend

they were laying people off," says Richard Broly, Sprint Corp.'s director of business in

## Special Report

Russia, the Mideast, and Africa. "It's a big political hotcake."

There is also the disquieting sense on the part of some nations that they are selling off a valuable piece of their patrimony to their former colonial rulers. "Countries are really struggling to come to grips with this situation right now," says Northern Telecom's Long. "They may have had outsiders in as consultants before, but never as owners."

Nationalism can slow development: China, long suspicious of outsiders, continues to ban any foreign equity ownership, operation, or management of its telecommunication sector. "Whenever I talk to the Chinese about foreign investment they say: 'Well, we're studying the issues,'" says Surinder Hundal, corporate relations manager for British Telecommunications PLC's Asia/Pacific operations. "The phone company is quite a valuable asset, and I think they would prefer to keep control in government hands."

**ONLY THE BEST.** China has, however, put the machinery in motion to bring in foreign assistance. It created a second phone company, Unicom, to challenge the Posts & Telecommunications Ministry's iron grip. Unicom has signed several memorandums of understanding with foreign companies that involve minority stakes. But, says one adviser, "they usually aren't worth the paper they're written on." Laments Ahmed Laouyane, director of the ITU's development bureau: "However much we try to narrow the development gap, local and international politics and policies will always be in the way."

Still, telecom is such a guaranteed moneymaker that few companies are willing to miss out—especially on the market the size of China or India or Indonesia. By 2000, 40% of the world's population will reside just in those three countries. Another prospect is Brazil. It has the ninth-largest economy in the world but a phone-line density of only 6.8 per 100 inhabitants. Russia holds enormous promise, too, pending the resolution of its many political and economic problems.

Beyond the giants, such countries as El Salvador and Bangladesh are seeking to develop their telecom networks any way they can. Even Africa, home to the world's poorest nations, is starting to attract some buzz (page 114).

None of these countries will settle for any old equipment though. Developing nations, unencumbered with decades-old copper wires, are installing digital switches, fiber-optic lines and the newest cellular technology. The most sophisticated networks in the world are in Djibouti, Rwanda, the Maldives, and the Solomon Islands, where 100% of the main lines are digital, compared with 49.5% in the U.S.

Advances in cellular technology also are showing up first in developing countries, because the technology allows them to put up a first-rate phone system in a matter of weeks or months rather than the years it can take to lay cable.

Telecom companies can try out such state-of-the-art technologies as digital satellite or fixed wireless, where the final link to the home in a fiber-optic network is a low-powered cellular connection, without having to worry about incorporating an existing huge network. Chile plans to throw the switch in December on a wireless personal communication service (PCS) network months ahead of the first U.S. system.

**PHONE LUST.** Foreign phone companies are often surprised by how quickly poor nations take to phone service. Put a phone in, and someone will call from it. No matter how poor when a country builds up its telecom network demand for phones and calling minutes rises. "Their willingness to pay for phones is far higher than anyone even thinks," says Roger A. Dorf, president of AT&T network systems in Latin America and the Caribbean. "It is always underassessed in every country."

For the world's telecom companies, then, the biggest problem is not

finding a place to invest but deciding which of the many places are the best. Gary M. Epstein, an international-telecom specialist at the Washington-based law firm Latham & Watkins, advises companies interested in buying into a developing country's newly liberalized phone market to first decide how much liberalization is enough. Most would prefer to avoid Chile's free-for-all and instead have competition phased in while they prepare the antiquated network for competition.

The toughest issue, though, is figuring out whether an investment opportunity is fairly priced. "You have to look at the

### Where The Growth Is

A guide to telecom hot spots

|                       | MAIN PHONE LINES*/<br>1993 | FORECAST<br>2000 | PROJECTED MAIN LINES<br>TO BE ADDED 1993-2000 | INVESTMENT<br>REQUIRED*** | CAGR** |
|-----------------------|----------------------------|------------------|-----------------------------------------------|---------------------------|--------|
| <b>ASIA</b>           |                            |                  |                                               |                           |        |
| CHINA                 | 0.98                       | 3.50             | 35.5                                          | \$53.3                    | 19.3%  |
| THAILAND              | 3.10                       | 9.35             | 4.4                                           | 6.6                       | 16.7   |
| INDIA                 | 0.77                       | 1.52             | 9.1                                           | 13.7                      | 11.2   |
| <b>EASTERN EUROPE</b> |                            |                  |                                               |                           |        |
| HUNGARY               | 12.54                      | 23.80            | 1.1                                           | 1.6                       | 7.8    |
| POLAND                | 10.28                      | 16.62            | 2.7                                           | 4.0                       | 6.7    |
| RUSSIA                | 15.28                      | 24.50            | 15.5                                          | 23.3                      | 6.7    |
| <b>LATIN AMERICA</b>  |                            |                  |                                               |                           |        |
| CHILE                 | 8.92                       | 19.71            | 1.8                                           | 2.8                       | 12.3   |
| BRAZIL                | 6.83                       | 9.49             | 6.8                                           | 10.2                      | 6.4    |
| MEXICO                | 7.54                       | 12.49            | 6.3                                           | 9.4                       | 8.5    |
| <b>U.S.</b>           |                            |                  |                                               |                           |        |
| U.S.                  | 56.49                      | 65.92            | 37.2                                          | 55.8                      | 2.9    |

\*A main line connects a subscriber to the central switch

\*\*Compound annual growth rate

\*\*\*All figures in U.S. dollars

DATA: PYRAMID RESEARCH INC.; INTERNATIONAL TELECOMMUNICATION UNION

A large, dark, jagged rock formation stands vertically against a clear blue sky. At the very top of the rock, a Mita DC-6090 copier is perched precariously, as if it were the only structure on the peak.

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WHETHER YOU'RE THERE OR NOT.**

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government's reason for selling," says Epstein. "There should be certain goals and targets, like the provision of universal service. If they're selling it just to make money, chances are it's not a good deal." Pakistan is often cited as a potentially bad deal. The government sold 10% of its phone company's shares to the public

## Special Report

last year and is now seeking a strategic investor. The government values its carrier at about \$8 billion. But with Pakistan's weak infrastructure, poverty, and political turmoil, "most of the world doesn't believe it," says Sprint's Brolly.

Even the best-assessed deals can turn sour. GTE, AT&T, and Spain's Telefónica have learned that lesson all too well. They spent \$1.8 billion for a combined 40% stake in Venezuela's monopoly phone company, CANTV. Last year, a financial crisis caused Venezuela's government to impose currency-exchange controls, preventing CANTV from making payments to foreign holders of its hard-currency debt. It defaulted, and the government reneged on a commitment to let CANTV raise phone rates every three months to keep pace with inflation.

**"PLEASE PRIVATIZE!"** Still, the foreign operators are hanging in. They just renegotiated CANTV's debt, and GTE says it was at the breakeven point on its investment at the end of last year. "You have to go at this with a mentality that you're going in there to stay, and ride over the rough spots," says AT&T's Dorf. "It's awfully easy to say things are tough in Venezuela and pull out, but then your credibility is shot in the rest of the region."

Not a good idea, given Latin America's enormous markets. Phone companies there are privatizing and liberalizing at a faster rate than in any other region, and welcoming foreign investment. The technical sophistication of networks is among the highest in the world. Telecom Argentina, the country's northern operator partly owned by France Telecom and Italy's STET, has plans to build a combination cable-TV/telephone network. Even Mexico's peso crisis, which rippled through the region, has failed to scare off investors. Bell Atlantic and SBC saw the value of their holdings plummet, but the crisis pushed the government to speed up liberalization to raise money. "You still have every major U.S. operator eager to jump into Mexico," says Linda Barabee, analyst with Pyramid Research.

Latin America's biggest prize—Brazil—is just about in reach. It has a growing economy, 156 million people—and a wholly inadequate phone system. Says former Finance Minister Mário Henrique Simonsen: "If you are in Rio and trying to call from Ipanema to the neighborhood of Botafogo, after 15 minutes of not getting through you want to scream,

'Please privatize the phone company!'" This August, the Brazilian National Congress voted to do just that, passing a law loosening state-owned Telebrás' monopoly and allowing private and foreign investment. Privatization of Telebrás' regional phone companies could begin in 1997.

First, though, cellular phones are likely to be opened to competition, creating eye-popping chances to make more. About 721,000 Brazilians have cellular phones, and 1.5 million are on waiting lists. The number of subscribers is expected to zoom to 6 million by 1998.

In Asia, while China and India crawl toward liberalization, other nations are bolting ahead. "When you look at India and China from a head-count perspective, they are clearly enormous," says Roy A. Scholvinck, the Los Angeles-based

director of global operations for EDS's management consulting group. "But when you look at the disposable income, it gives you a different perspective."

Indonesia's perspective, for example. The nation's 190 million has twice the per-capita GDP of China and wants to install 5 million phone lines over the next

## Countries are throwing open their doors to foreign operators and equipment makers—and the competition is wicked



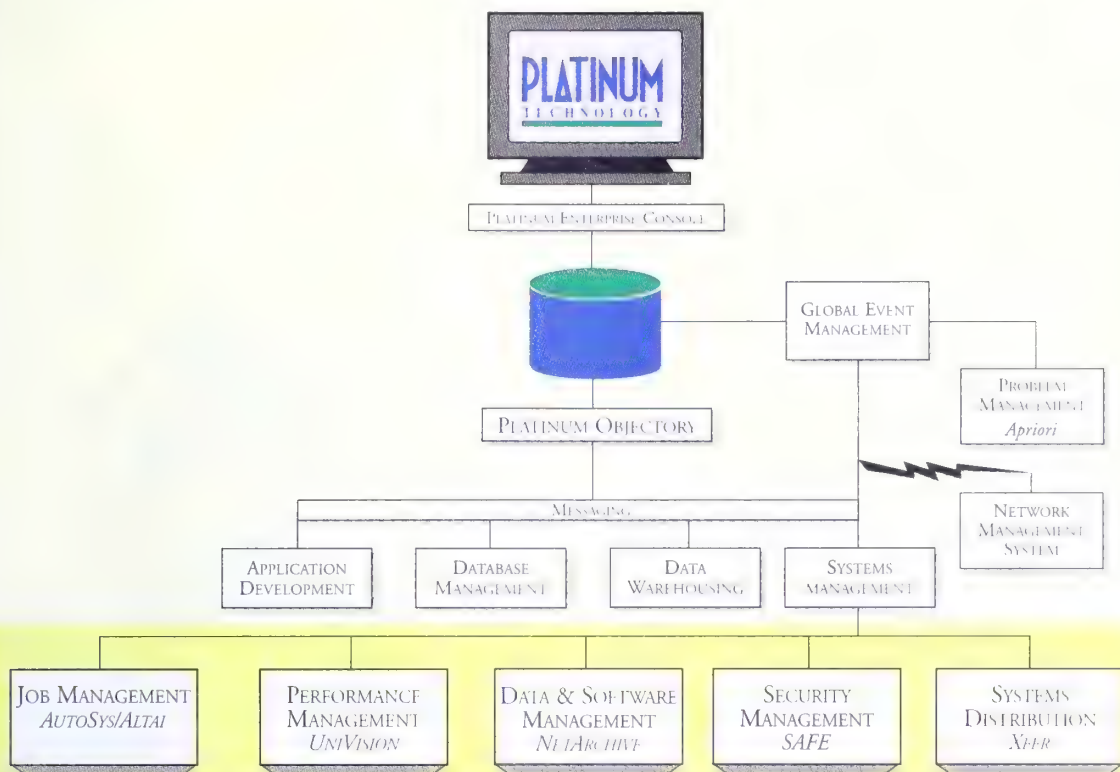
**BUENOS AIRES CHAT:** Latin American telecoms are privatizing faster than anywhere else

years—at a cost of \$6.8 billion. The country opened its market to competition last year, and 30 different international consortiums submitted bids. State-owned telephone company PT Telkom selected five consortiums this past June, led by Nippon Telegraph & Telephone, Telekom Malaysia, Singapore Telecom, France Telecom, and Australia's Telstra, to build and operate the networks for 15 years. Significant bids were eliminated after they failed to submit the highest bids, a harsh brush with fairness.

Foreign investors are also eyeing the former East Bloc. But the enthusiasm that erupted after the fall of the Berlin Wall has dampened. Changing political regimes have slowed the decision-making process to a standstill. There have been five different post and telecom ministers in Poland and the same has been similar turnover in the other new democracies—

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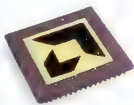
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each change has been accompanied by a new plan.

Financing is another huge problem. Phone tariffs in some former Soviet republics are nonexistent because of a lack of billing equipment, so the regions can't pay for any massive

## Special Report

improvements themselves. Siemens still manages to do "several hundred million marks" per year of business in the region, says Jürgen Lagleder, head of public telecom sales for Siemens, but not all of it is exactly liquid. Siemens sold a telephone exchange to a lo-

cal government in Russia on the Caspian Sea recently—for million worth of caviar.

Still, not a bad deal if you like caviar. And once the government gets a modern telecom infrastructure in place, it might start exporting its own caviar and use the money to buy more phone lines. It's a vision that all developing countries share, in one form or another, and if it happens, it should shake the entire global economy. Wouldn't it be nice if every country could phone home?

*By Catherine Arnst in New York, with Susan Jackson in Santiago, Michael Shari in Jakarta, and bureau reports*

# HELLO, AFRICA? HAVE WE GOT PHONES FOR YOU

A year ago, 30-year-old Nomonde Ntontela was an out-of-work cashier when she heard that Vodacom, one of South Africa's cellular operators, was looking for entrepreneurs to operate "phone shops" in black townships and squatter camps. Today, customers line up outside her business—a specially outfitted shipping container with five metered cell phones, set down in one of the most squalid sections of Alexandria.

Ntontela's customers include illegal aliens from Mozambique and parents who have left their children in rural villages to find work in the city. Private phones are virtually nonexistent in the townships; before Ntontela's shop opened, residents paid nearly \$1 to take a minibus to the other side of town. The phone shop in their neighborhood, one of thousands built by Siemens, Alcatel Alsthom, and other suppliers for underprivileged areas, is clearing almost \$2,500 a month. Ntontela nets about \$800 after paying cellular charges, a small fee for the franchise, and her one employee. "I don't have financial problems anymore," she says—and she has started saving for a second shop.

**RINGING THE CONTINENT.** No question, this telecom wasteland is ripe for development. There are only 0.8 main phone lines per 100 people in all of sub-Saharan Africa—in rural areas, whole villages are without phones. Increasingly, African nations realize that their future development depends in part on connecting to the global phone network.

Money is the obstacle. African countries will need a lot more money than Western development agencies can provide. So they're cracking open phone markets to competition, pri-

vatization, and foreign ownership. Uganda, the Congo, and the Côte d'Ivoire have announced plans to privatize their phone companies in 1996, while Tanzania recently agreed to establish a second phone company, a first for Africa, with foreign ownership allowed.

But it's two megaprojects that are putting Africa on the radar screens of the world's telecom companies. South Africa, to redress decades of

E-mail service, Uninet, pays \$150,000 a year for an Internet link that would cost \$5,000 in the U.S. "We think there is a huge untapped communications need," says William B. Carter, president of AT&T's submarine-cable unit. "As soon as the cable goes in, the price will drop, and demand should explode." International carriers eager to get a share of those future calls are financing 70% to 80% of Africa One.



**FEW CONNECTIONS:** Pay telephones in a township outside Pretoria, South Africa

inequitable development, plans to spend more than \$1.6 billion to build 1 million main lines in mostly black rural areas. Telkom South Africa received bids from 22 consortiums, many led by foreign telecom companies, and plans to award the contract in 1996.

The entire continent could get a boost from the second project: Africa One. This consortium, led by AT&T, plans by 1999 to ring the continent with an undersea cable, giving each nation a direct link to outside. Now, few African countries can dial one another directly—intraregion calls are typically bounced back via satellite from Europe. International calls cost about \$10 a minute; a Zambian

Getting financing for other African projects has been tougher. But that may be changing, says Bert de Grave, head of international operations for Alcatel, a longtime supplier to Africa: "South Africa's opening up gives a certain comfort level to foreign investors." To promote more investment, the U.S. Agency for International Development has started a \$75 million program to help African countries with regulatory reform and other changes. "The region is ready," says Wade Warren, director of the program. Increasingly, foreign phone companies are, too.

*By Drusilla Menaker in Johannesburg, with Catherine Arnst and Deborah Steinhorn in New York*

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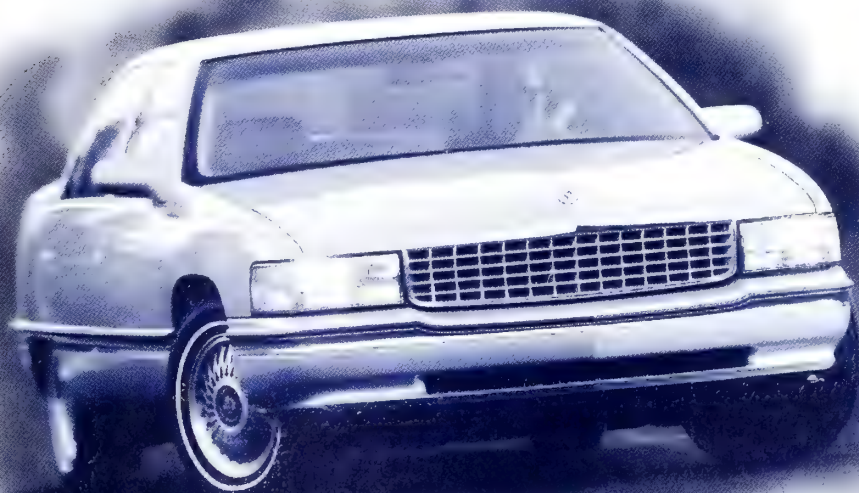
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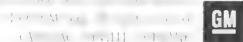


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## CHEMISTRY

# SWAPPING A TEST TUBE FOR A SHOTGUN

Concocting millions of compounds simultaneously could speed up drug discovery

**B**ack in the mid-1980s, Australian scientist H. Mario Geysen was a prophet without a following. He had figured out a way to rapidly combine molecular building blocks in many different ways—an approach known as combinatorial chemistry. While conventional chemists could synthesize only a few dozen druglike compounds a year, he could churn out thousands of protein fragments called peptides in a few weeks. That offered a possible cure for one of the pharmaceutical industry's biggest headaches: discovering new drug candidates. The industry's response? A resounding yawn. "We couldn't get the message across," recalls Geysen.

Today, nobody is yawning. Geysen is now a drug-discovery chief at Glaxo Wellcome Inc., his former company is a division of biotech powerhouse Chiron Corp., and once neglected combinatorial chemistry is on its way to becoming the drug industry's hottest new tool. "Not since recombinant DNA [gene-splicing] have I seen a technology catch on so fast," marvels Isis Pharmaceuticals Inc. Vice-President David J. Ecker.

Indeed, drug giants

such as Merck, Pfizer, and Chiron have set up major in-house efforts, while others rush to buy companies specializing in combinatorial approaches. In the past year, Marion Merrell Dow Inc. snapped up Tucson-based Selectide Corp. for \$58 million, Glaxo paid \$538 million for Affymax, based in Palo Alto, Calif., and Eli Lilly acquired Sphinx Pharmaceuticals in Durham, N.C., for \$72 million. Add in such startups as Pharmacopeia in Princeton, N.J., ArQule in Medford, Mass., and CombiChem in La Jolla, Calif., and there may be more companies doing combinatorial chemistry than Wall Street analysts who understand the new technology, jokes David K. Stone, managing director of Cowen & Co. Says Martin F. Haslanger, president of Lilly's Sphinx subsidiary: "I don't know of any big pharmaceutical company that doesn't have, or isn't scrambling to get, a major combinatorial chemistry effort."

The reason is the sheer difficulty of

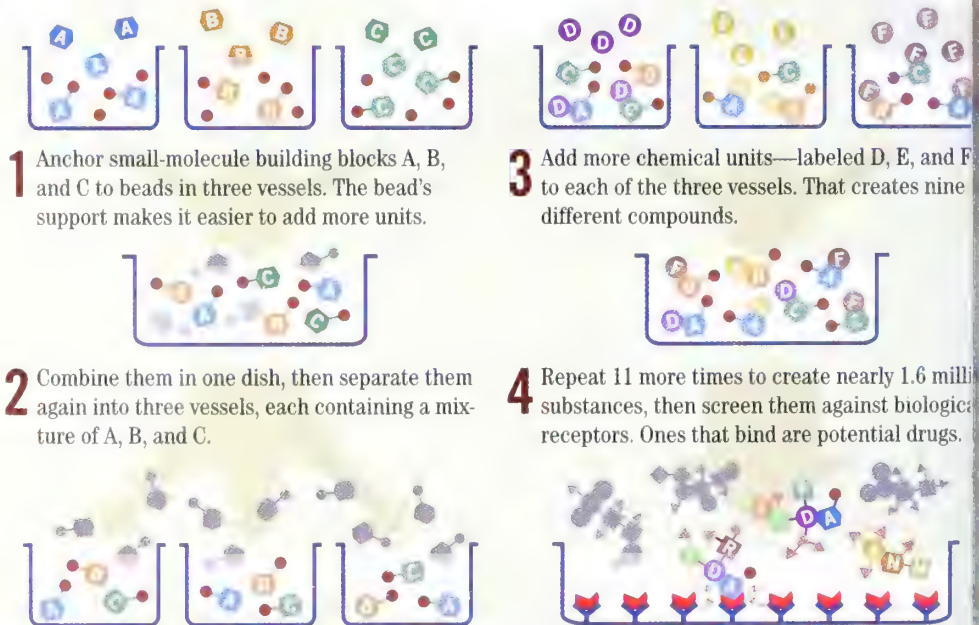
discovering new drugs. In today's typical approach, a company starts with a element in a biological pathway—an enzyme involved in heart disease, for example, or a cell receptor that signals the immune system to fight cancer. The trick is finding a chemical that binds to these enzyme or receptor "targets," turning them on or off to treat an illness. Historically, the odds of finding a blockbuster drug weren't much better than those of winning a lottery.

**COMBINING NATURE.** Over decades, drugmakers have painstakingly synthesized hundreds of thousands of chemicals—one at a time. They are combining the natural world, from rain forests to marine life, for new compounds. And recently they've developed automated methods for rapidly testing thousands of chemicals against molecular targets. The problem is, the drug hunters still aren't catching up with many winning lottery tickets. "We have targets we know are important but haven't been able to find molecules

## THE MAGIC OF COMBINATORIAL CHEMISTRY

*Traditional drug chemists labor for days to synthesize and analyze a single new compound. With combinatorial chemistry, a highly automated laboratory can produce and screen 1 million new compounds in weeks.*

DATA: PHARMACOPEIA, CHIRON, BUSINESS WEEK







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## The approach isn't limited to drugs: Materials scientists are finding applications in superconductors and chips

that will interact with them," admits Paul Armond, Pfizer's assistant research and development director. And now that gene sleuths and molecular biologists are finding thousands of new targets, the challenge is greater than ever.

Hence the immense allure of combinatorial chemistry. Glaxo's Geysen estimates that the nascent technology already has produced more new compounds in just a few years than the pharmaceutical industry previously did in its entire history.

What's more, the combinatorial approach isn't limited to drugs. At the University of California at Berkeley, chemist Peter G. Schultz and colleagues are making 10,000 new materials in single experiments. The approach, Schultz predicts, may be the key to discovering everything from new semiconductors to superconductors. Already, he has uncovered a new material with special electromagnetic properties and founded a company, Symyx.

**"LIKE BLASPHEMY."** The combinatorial idea comes not from chemistry, but from the immune system's ability to churn out many types of antibodies. "To the classic organic chemist, this is like blasphemy," says Scripps Research Institute chemist and molecular biologist Kim D. Janda, founder of CombiChem Inc. While chemists pride themselves on meticulously purifying and analyzing each chemical compound separately, combinatorial chemistry uses a shotgun approach. The basic idea: produce huge numbers of compounds almost at random by shuffling around molecular building blocks. Only when a chemical shows interesting biological activity do scientists go back and figure out the composition. It's such a simple idea that "we look back and say, 'My God, why didn't we see this 20 years ago?'" says Walter H. Moos, vice-president for R&D at Chiron.

The main reason for the slow uptake: Combinatorial chemistry's pioneers, such as Geysen and Affymax, initially fashioned only peptides and oligonucleotides, which are compounds made from the building blocks of DNA. Not until the early 1990s, when scientists such as Berkeley chemist Jonathan A. Ellman

were able to synthesize collections of small organic molecules—the typical raw material for drugs—did most of the pharmaceutical industry take notice.

Despite the enthusiasm, there are raging debates over the best combinatorial approach. Perhaps the most common tack, used at Pharmacoepia, Chiron, and other companies, is a "pool and split" strategy. Chemists begin by anchoring different molecular building blocks to solid supports (typically plastic beads) in



**PRINCE OF PEPTIDES:** Chiron's robotic chemical-synthesis gear

each of several containers (diagram, page 116). They mix the compounds together, then divide up the pool. Chemists then add a second chemical unit—a different one to each container—and pool and split again. Repeating this a number of times can create millions of different compounds in a handful of containers.

If one of the compounds "hits" a biological target, chemists must then go back and figure out the composition of the chemical. One clever solution is using molecular tags, much like a bar code, that keep track of each compound's structure. But many chemists think the pooling and tagging strategy is too complicated. That's why Merck, CombiChem, and others are making thousands of compounds simultaneously but separately, using robots to deliver building blocks to each vial in different order. The most exotic version of this method comes from a collaboration between the David Sarnoff Research Center and SmithKline Beecham. Sarnoff scientists plan to put 10,000 microscopic test tubes, along with

a maze of hair-thin channels, pumps, sensors, on chips the size of business cards. Not only could such chips make 10,000 molecules in a few hours, but they can also use them to screen the molecules against our biological targets," says SmithKline R&D chief George Poste. **NO MIRACLE CURE.** Whichever method prevails, many industry experts think the payoff from combinatorial approach will be huge. Indeed, drugs produced this way are nearing clinical trials. I

hopes to start testing a central nervous system drug this year. Isis is excited about an anti-AIDS compound.

Combinatorial chemistry, though, is no miracle cure for the ills of drugmakers. Companies have learned that simply making racks of compounds isn't enough, says Columbia University chemist W. Clark Still, founder of Pharmacoepia. "You have to make huge quantities of carefully chosen molecules," says. And to become drug compounds also must be relatively nontoxic, get into the right cells, and stick around the body for the right amount of time. That's why drugmakers are also beginning to

multaneously test the new chemicals. Such practical considerations as absorption across the stomach wall. "The combinatorial chemistry bandwagon has a lot of people riding on it," warns Geysen. "But few appreciate what it takes to make it practical."

Still, even skeptics agree that it may be the best hope for finding truly novel drugs for previously intractable diseases. And once a potential drug is found, the technology can quickly generate its possible relatives, increasing the chances of finding the best version and helping a company stake out a strong patent position.

The bottom line: Combinatorial chemistry could transform drug discovery and new material synthesis, much as gene splicing stood modern biology on its head. "It's a revolutionary technology," says biochemist James Rothman of the Memorial Sloan-Kettering Cancer Center. All companies need to do is figure out how best to use it.

*By John Carey in Washington*





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## A MINERAL ANTIDOTE TO GLOBAL WARMING

NO ONE IS SURE JUST HOW serious the "greenhouse effect" is. But if scientists conclude that a further buildup of carbon dioxide gas in the atmosphere will cause a big increase in global temperatures, a Los Alamos National Laboratory team stands ready with a costly but effective solution.

Los Alamos physicist Klaus S. Lackner says it should be possible to separate carbon dioxide gas out

of the smoke from fossil-fuel-burning plants, and then mix it with certain minerals such as magnesium oxide or calcium oxide, probably at high temperatures. Carbon in the gas would permanently bind to the minerals, keeping it out of the atmosphere. Lackner estimates it would cost about 5¢ to soak up the carbon dioxide formed in the production of a single kilowatt-hour of electricity—figuring in

everything from construction of treatment plants to mining and crushing the mixing ores. That's equal to the roughly 5¢ per kilowatt-hour to produce the electricity in the first place.

Still, that would be cheap if the alternative is having the polar ice sheets melt and flood coastal cities from New York to Tokyo. Says Lackner: "I view this as an insurance policy." A scholarly paper on the subject has been accepted by *Energy*, the *International Journal*.

## ALL THE RIPCORD, AND THE PLANE LOADS DOWN

SENIOR EXECUTIVES MAY have golden parachutes to soften their landings, but any manager who pilots a private plane can soon get something even more comforting: an aircraft parachute. No need to jump to use it—this chute, which weighs just 80 pounds, lowers the entire airplane slowly to the ground. It will be the main safety feature on Cirrus Design Corp.'s SR20, the first plane certified by the Federal Aviation Administration to come equipped with its own safety net. And this is

no ultralight experimental plane: The SR20 is a four-seat aircraft with a 200-horsepower Teledyne Continental Motors engine that provides a cruising speed of 160 knots (185 mph).

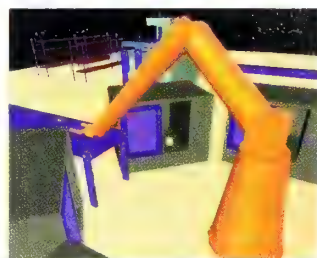
Expected to go for \$130,000 when it's introduced in 1997, the single-engine SR20 aircraft has an all-composites airframe also designed for safety. The structure is engineered to



protect people in the cabin area by deflecting the initial impact and absorbing shock, should a mishap occur at an altitude too low to deploy the chute.

Cirrus Design has been developing the SR20 since 1990. The prototype plane made its maiden flight on Mar. 31. Now, the Duluth (Minn.) company is raising \$10 million to complete the required flight tests and start up production.

## INNOVATIONS



■ Mechanical engineers at the University of Illinois at Chicago are building a virtual factory (above). By donning special glasses and gazing at 4-by-6-foot displays laid out like drafting tables, plant managers in different cities will be able to convene, inspect moving machinery, and share 360-degree views from any location on the factory floor.

■ NEC Corp. has built a snake-like inspection robot that will slither through the rubble of collapsed buildings to find survivors. An "active universal joint" allows up-down and left-right movement for each of the snake's segments.

■ Catheters and endoscopes let doctors peek inside patients' bodies. But one day, computer software could provide new glimpses noninvasively. Pennsylvania State University electrical engineer William E. Higgins and VIDA Technologies Inc. in Iowa City, Iowa, are creating moving images of patients' airways and digestive tracts by digitally compiling data from CT scans.

## ONE GIANT STEP FOR GELS

THERE'S NOTHING STRANGE about Jell-O congealing when the mercury drops. It is trickier to make a gel that hardens in heat and turns back into a liquid when cooled. Massachusetts Institute of Technology physicist Toyochi Tanaka has spent most of his 20-year career researching such unusual polymer gels. His patented "smart hydro-

gels" jump through phase changes, shrink down, or expand thousands of times in response to changes in temperature, light, electric or magnetic fields, or chemical stimuli.

These aren't idle parlor tricks. The company Tanaka co-founded in 1992 in Bedford, Mass., called Gel Sciences Inc., will soon start spinning gels into commer-

cial products. First out the door, in mid-1996, will be a golf shoe designed with partner Titleist & Foot-Joy Worldwide in Fairhaven, Mass. A gel in the shoe upper warms to the wearer's body temperature and matches the contours of the wearer's foot: If that aching foot starts to swell, the shoe adjusts.

Next, the company's medical subsidiary, called GelMed, will seek Food & Drug

Administration approval to test therapeutic and cosmetic gels. One of these, a "reverse" thermal gel that is liquid at room temperature and viscous at 98.6 degrees, could be used to deliver eye medications. A few drops would spread evenly over the eye to form an ultrathin liquid sheath, allowing for continuous, slow release of a drug. GelMed is in early discussions with several drug companies.

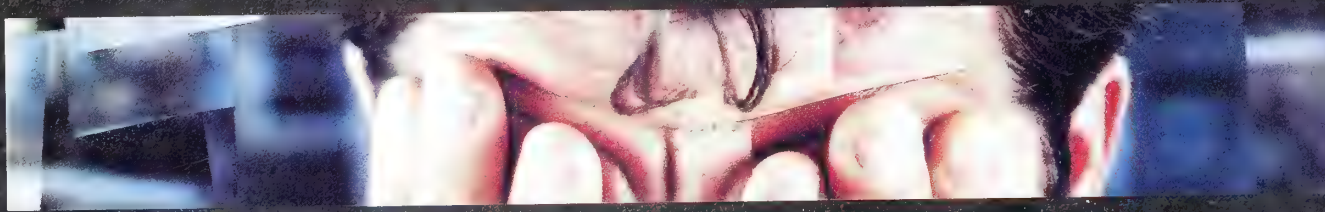




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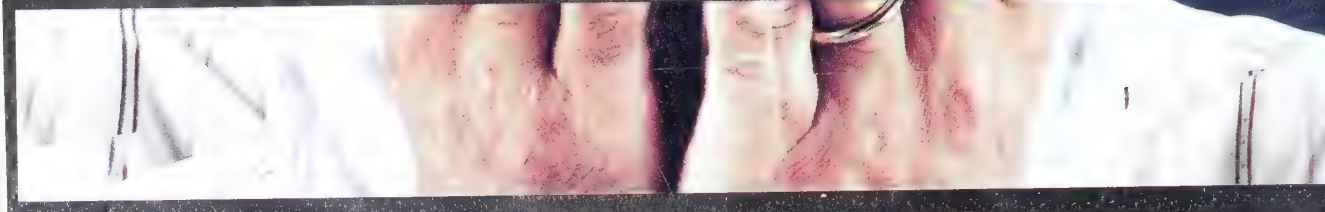
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# MANAGEMENT

Once every month, the top officers of the company gather around a large conference table to discuss the most intimate details of operations. They reveal profit and sales figures, work in progress, and incoming orders. Sitting in the audience—yes, the audience—are more than 40 managers from such companies as Digital Equipment, Mobil, Eastman Kodak, and Union Pacific.

They are here, at itty-bitty Springfield ReManufacturing Corp. in the Ozark mountains of southern Missouri, to

learn about a concept called "openbook management," which has propelled this private, \$104 million company to cult status in business circles.

Over the years, more than 2,400 outsiders have trekked to Springfield, Mo., to stroll through a gritty plant where workers reassemble diesel engines and to sit in on the 90-minute meeting.

Springfield is just one of many management meccas visited by tens of thousands of acolytes every year. Medieval pilgrims, beset by pestilence, war, and famine, sought serenity and certainty at Canterbury, Santiago de Compostela,

or Assisi. Today's corporate palmers, ravaged by the maelstroms of globalization, downsizing, and technological change, look for solutions and security at Motorola, Microsoft—and Springfield Re. Some 2,000 devotees stream through AT&T's Universal Card's superefficient telephone customer service center in Jacksonville, Fla., every year, at \$375 a pop. More than 5,000 supplicants have sojourned at Federal Express' expansive overnight package facility in Memphis for a \$200 midnight hub tour and all-day seminar. USAA, the San Antonio-based insurer, has drawn more than 2,100 seekers to its monthly program from such far-flung locales as Australia, Italy, Japan, South Korea, and South Africa.

**"GOGGLE-EYED."** They come for inspiration, for ideas, and for fun. "People run through some of these companies' showcases, as if they were theme parks for management," says Gerald Ross, co-founder of Change Lab International, Stamford (Conn.) consulting firm. "They come out of the places goggle-eyed."

More is going on here than sightseeing, though. The visits usually represent a serious effort to absorb what works at the best companies in the hope of applying those precepts back home. The phenomenon also reflects a sharp change in perceptions of the health of Corporate America. It's the standard U.S. success stories that are drawing most of these wander-

## Cover Story





# MECCAS

Everyone seems to be studying U.S. corporate stars

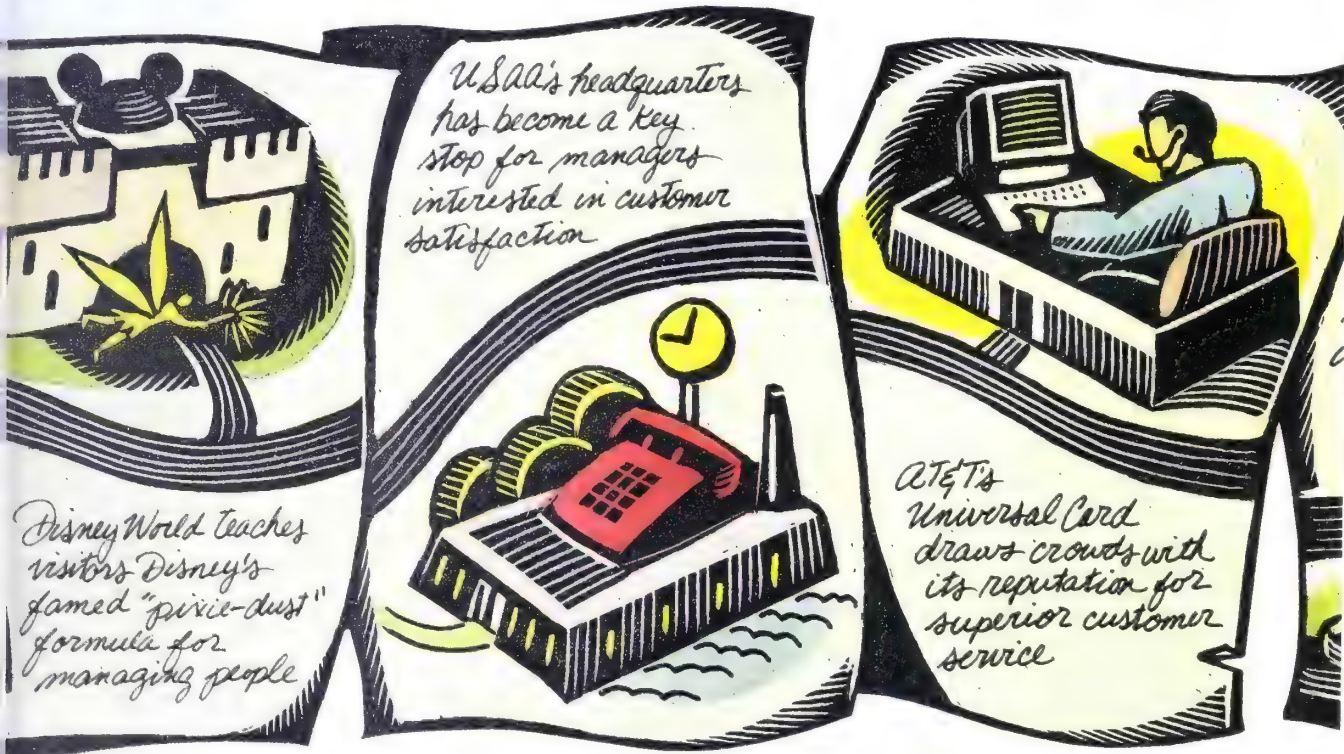
managers—in contrast to the mid-1980s, when plane-jets of executives, fretting about declining U.S. competitiveness, routinely traveled through factories in Japan in search of ideas. "There's a lot more in America to see and digest than there has ever been before," says Norman Bodek, president of Productivity Inc., a firm that organizes industrial visits. This year, Bodek will lead only one study mission for managers to Japan, down from six or seven a year in 1985 and 1986. The intense interest in examining the best that American industry has to offer is an outgrowth of the benchmarking movement of the early 1980s, and it's yet another example of a thriving marketplace for business ideas. To become more efficient, executives are gobbling up business books, hiring consultants, and paying greater attention to the expanding roster of management gurus. It's only natural that they would try to learn from one another, too.

What is it about these cult companies that draws so much attention? Each of them has gained a reputation for excellence in something, whether it's superb customer service or true product innovation. Some offer visitors the opportunity to observe how a vogueish concept, from "open-book management" to "self-managing teams," works in practice. Almost all of these organizations have gained outside recognition, by winning plaudits from a management guru or the media, by

capturing a Baldrige Quality Award, or simply by earning the admiration of competitors for solid records of profitability or revenue growth.

Like any human enterprise, they can stumble, and their cult status may be fleeting. For years, hordes of visitors roamed through Stew Leonard's supermarket in Norwalk, Conn., which had been hailed by management guru Tom Peters as a model of customer-focused retailing. Managers from Citicorp, Procter & Gamble, and IBM flocked to the circuslike store with its singing, mechanized farm animals and petting zoo. "The store became a hot spot, particularly for the Japanese," recalls Peters. "They came by the jillions"—until 1993, when the company's folk hero and founder, Stew Leonard Sr., was sentenced to four years in prison for his role in a tax-fraud scheme. The company says visits have since rebounded. And despite a recent earnings plunge at Rubbermaid Inc. (page 80), the company remains a magnet for executives hoping to pick up a little of its new-product magic.

Most managers yearn to visit the headquarters and plants of high-profile corporations—the likes of Motorola, Hewlett-Packard, Microsoft, and Wal-Mart. No surprise there. But these pilgrims also wind their way to much less familiar sites, such as Springfield Re and Johnsonville Foods, a Sheboygan (Wis.) sausage maker, where they learn how "self-





managing teams" have transformed a floundering family business into a dynamic, fast-growing company. "At first, I couldn't believe that anyone would be interested in what some sausage company in Wisconsin was doing," says Ralph F. Stayer,

Johnsonville's CEO. "But it has been truly amazing."

Johnsonville's Stayer and Springfield ReManufacturing's CEO, Jack Stack, have become widely quoted gurus in their own rights, thanks to their companies' fame. They've written business books, they tour the lecture circuit, and they spend several days a week consulting while still holding down their jobs. Stayer averages 25 speeches a year. Stack says revenues from Springfield's "Great Game of Business" tour, videos, books,

and consulting business will hit \$1.8 million this year.

Yet another cult company off the beaten path is Lincoln Electric Co., a Euclid (Ohio) maker of arc welders and welding supplies that has long been considered a model of how to motivate employees and hike productivity. Since 1983, nearly 12,000 outsiders have visited Lincoln's headquarters and factory to learn about the company's innovative incentive plan. General Motors Corp. alone has sent more than 120 people to Lincoln Electric, and GM's Saturn unit has publicly acknowledged that it has borrowed some ideas from the company.

So widespread has the company tour become that some consulting firms, including Boston Consulting Group Inc. and CSC Index Inc., now commonly use such on-site visits as a key part of their problem-solving methodologies. Management teams in the midst of efforts to revamp their own companies

## Cover Story

# A TOUR GUIDE TO MANAGEMENT MECCAS

*Dozens of U.S. companies now offer formal workshops, seminars, and tours for outsiders who want to know how they manage employees and operations. Here's the rundown on some of the most popular places.*

## AT&T UNIVERSAL CARD

**PROFILE PROGRAM** Day-long program and tour of customer service center handling 1.5 million calls a month. Features lively and candid presentations by managers from departments of information services, quality, customer relations, and human resources. There's also a gee-whiz demo of Universal's high-tech systems, which allow employees to pull up complete records on customers calling in even before the staffers pick up the phone. Buffet lunch in company cafeteria features managers and/or employees at each table. Day ends with Q&A session with a top executive. Maximum group is 25; held every Tuesday and Wednesday.

**COST:** \$375 (\$285 for nonprofit visitors)

**CONTACT:** Paula Chaon, Jacksonville, Fla. 800 682-7759

## WALT DISNEY

**DISNEY'S APPROACH TO PEOPLE MANAGEMENT; QUALITY SERVICE;**

**CREATIVE LEADERSHIP; ORIENTATION** Your children will envy your visit to these business briefings by Disney: Each of the four core programs includes passes to Disney's theme parks. In the People Management seminar, Disney managers explain the company's "pixie-dust" formula for managing and tell how you can sprinkle it on your own organization. Theme park managers do

most of the presentations. There's even a tour of Disney's hi-tech infrastructure, the six-acre underground tunnels beneath the Magic Kingdom. Maximum group size is 70; held at least monthly.

**COST:** \$2,295 for 3½-day sessions, including three nights at a Yacht Club or Contemporary Resort hotel and free passes to Disney's theme parks; \$1,480 for 2½-day orientation seminar.

**CONTACT:** Disney University Professional Development Services, Lake Buena Vista, Fla. 407 824-4855

## FEDERAL EXPRESS

**FEDERAL EXPRESS QUALITY FORUM** Night owls will love this intriguing glimpse into FedEx's expansive package-handling facility. The hub tour begins at 10:30 p.m., just as planes are descending here to drop off and load packages for next-day delivery. The next morning, visitors hear managers discuss the company's "people-service-profit" philosophy as well as its human-resource and customer service policies. A vice-president spends an hour before lunch answering questions. After lunch, members of a "quality action team" discuss their work. FedEx ends the day with a highly popular session on how it measures service quality. Maximum group size is 35; held twice monthly. Special group forums also available.

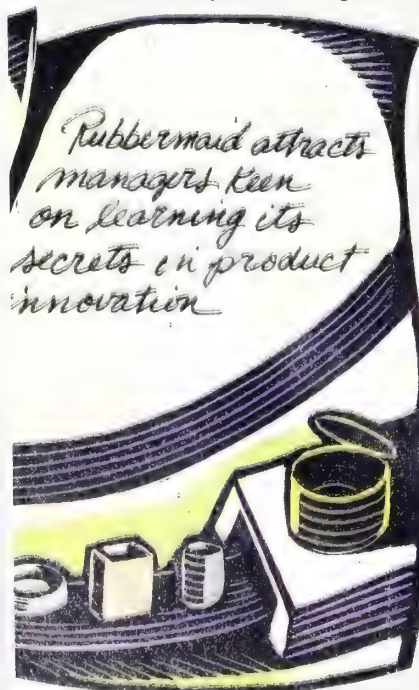
**COST:** \$250, including lunch and the late-night hub tour

**CONTACT:** Dolores Green, Memphis 901 395-3461

## JOHNSONVILLE FOODS

**LEADING THE JOURNEY** Full-day workshop begins at 8:30 a.m. over coffee and sweet rolls at City Streets, a local restaurant on the Lake Michigan waterfront. There's an hour-long slideshow on the company's move to self-managing teams before the program highlight—a freewheeling two-hour session with five employees and managers. The picnic lunch features Johnsonville bratwurst and Italian sausage. Afternoon session explores the company's incentive-pay plans and mistakes. Ends at 4 p.m. Drawbacks? The restaurant is the closest you get to Johnsonville, located six miles away. The company stopped offering plant tours after employees complained that chats with outsiders prevented them from doing their work. Maximum group size is 25; workshops are held monthly.

**COST:** \$235, including lunch and a copy of CEO Ralph Stayer's book, *Flight of the Buffalo*





tinily visit dozens of these shrines before tackling their n transformations. Groups of managers from Nynex Corp., example, recently visited an astounding 152 separate npanies, including British Airways, MCI, and Roto-Rooter, glean workable ideas that they could apply to a major re-engineering effort. Managers from GTE Corp. raced through 80 npanies for the same purpose in the summer of 1992.

**ELING THE FABRIC.** Proponents of the corporate *hajj* say h trips allow them to see how various strategies work in ctice, rather than merely consider a new approach in the stract. "You get a real sense for the culture of a company, what the people are like and what the place ks like," says Jay Michaud, a vice-president h csc Consulting. "There is a real thirst and ed for these visits because most of the innova-

tion in business today is happening in the field." As William LeStage, a Nynex assistant vice-president, puts it: "You get to know what kind of wood it takes to make shingles, and what kind of leather you need to make shoes."

Visits to AT&T Universal Card, Delta Air Lines, and GE Credit, for example, convinced LeStage and his colleagues that large service centers—with 1,500 to 2,000 employees—boasted far greater efficiencies and competitive advantages than did Nynex' smaller centers, which average 55 employees each. "It's much more difficult to change pricing policies or launch new products when you're dealing with hundreds of work centers," says Le-Stage. Nynex is now consolidating 374 customer-contact centers with a total of 20,500

CT: Elaine Crawford, Sheboygan, 44 459-7139

## MOTOROLA

**MOTOROLA'S QUALITY BRIEFING** Aficiona-the quality movement have made op a must. This eight-hour seminar es managers with an inside glimpse of otrola created and manages its Six quality culture. The session also in-segments on "total cycle time reduc-und "total customer satisfaction." In ernoons, visitors hear how Motorola 'sity spreads the quality gospel. The gs have become so popular that Motor-en brings the show on the road (this o hotels in Phoenix and Austin). An added bonus: limited time, Motorola is giving the first 50 partici-a free cordless telephone. Held eight times a year.

\$395, including continental breakfast and lunch

ACT: Abbi Sedivec, Schaumburg, Ill. 708 576-7917

## SATURN

**SATURN PLANT TOUR AND PRODUCTIVITY'S HIGH-IRMANCE WORKSHOP** For car buffs and manufacturing you can't beat this two-day program featuring a tram f General Motors' innovative Saturn factory. The pro-s focus is on employee involvement and "visual con—a way to organize a factory more efficiently. The morn-ur is followed by lunch and a Q&A session with two or Saturn employees who describe their team-based ap-h to work. After the first day, visitors hole up in a local for a workshop in Japanese manufacturing concepts and hey relate to the Saturn experience. Maximum group : 60; held once a month.

\$895, including lunches and "high-performance produc-workshop by Productivity, Inc.

ACT: Maureen Fahey, Norwalk, Conn.

46-3777. Saturn tour in Spring Hill, Tenn.

## SPRINGFIELD REMANUFACTURING

**GREAT GAME OF BUSINESS** Two-day seminar on "open-management" begins with story of company's spin-off International Harvester and the decision by owner-man-



agers to train employees to understand the company's financials and to share that data with them on a regular basis. Visitors are shuttled from the headquarters building to a gritty plant where engines are remanufactured. The day's highlight: Guests are allowed to sit in on the monthly meeting at which the company's managers and employees go over all the numbers. "Nobody holds back even though we have visitors here," says CEO Jack Stack. "You can't. The numbers have got to come out. And you see the anger, frustration, and humor of it

all." Maximum group size is 50; seminars are held monthly.

**COST:** \$1,250, including two nights of lodging, all meals, and an autographed copy of Stack's book *The Great Game of Business*

**CONTACT:** Charlotte Ecksley, Springfield, Mo. 800 386-2752

## USAA

**THE QUALITY JOURNEY** Who said you can't get a free lunch anymore? This private insurance company not only feeds visitors breakfast and lunch but doesn't charge for its day-long program. A company van even picks up guests at a local Marriott at 7:50 a.m. and returns them at the end of the program at 5:15 p.m. The morning sessions focus on the company's employee-friendly culture, its emphasis on customer satisfaction, and its "continuing strides to excellence." Visitors walk through the largest private office building in the world to one of five cafeterias for lunch with a USAA executive. In the afternoon, they attend one of three breakout sessions on information services, customer service, or human resources and training. "What really wows them is the building," says a USAA spokesman. "I don't care if they are from IBM. No one has ever seen a building so intelligently designed for employees." Maximum group size is 60; no more than three visitors from one company at any time; program is held monthly.

**COST:** Free

**CONTACT:** Angelo de Guttadauro, San Antonio 210 498-0902



## Cover Story



employees into 53 with 14,700 employees.

Managers keen to implement a new idea also want to talk to others who have been through the experience. "Everybody just wants to see something working," says Springfield Re's Stack. "Before they buy another car, they want to see the engine is there and the tires are brand new. They come in here and look under the hood, and they have a revelation."

**PONY SHOWS?** Some critics, however, charge that these "best practice" workshops and visits are so brief, superficial, and stage-managed that they amount to little more than industrial tourism. Teams of managers often jump from one company to the next, delving no deeper than the jet-lagged traveler on a seven-countries-in-seven-days tour. Skeptics also charge that companies try too hard to put on a carefully prepared show that's long on hoopla and short on reality. "Many of these companies aren't as good as they are cracked up to be, so you're getting packaged answers and the party line," says Change Lab's Ross. "When you have a few beers with a manager late in the evening, you usually find out the real story." Another consultant, paid to lead a group of BellSouth Corp. managers through Intel Corp., jokes that the highlight of their visit was a sighting of Intel CEO Andrew S. Grove with Microsoft Chairman William H. Gates III in the company cafeteria.

Even so, most managers who travel this business circuit do so to lay the groundwork for major changes in their own organizations. Earlier this year, for example, a group of 21 "change agents" from Munich-based Siemens Nixdorf came to the U.S. to make the rounds. Each manager, selected by the board of directors, has been charged with a specific mission, from helping launch a business unit to increasing international sales for Europe's second-largest computer maker. Members of the group visited 50 U.S. companies, studying

## BY THE NUMBERS

### Springfield ReManufacturing spreads the gospel on sharing key information with workers

**SAFETY FIRST: REBUILDING  
A DIESEL ENGINE**

operational efficiency at Feder Express Corp. and product leadership at 3M. "The visits were exceptionally fruitful," says Tyrone Morris, a Siemens Nixdorf financial controller whose title is not "change agent."

Morris' task is to help Siemens create an information-systems outsourcing business. So he also visits several outsourcing companies, including Roadway Logistics Systems, which has taken over distribution for Dell Computer. "My strategy was to learn and learn and learn

says Morris. "We discussed lots of ideas, and we built up a network of people to rely upon in the future. I've already called some of the people I met on the trips for advice. One contact, for example, informed him of the steps necessary to develop the best sales prospects for outsourcing.

How much of what they learn can managers actually apply to their own companies? Sometimes, not much—especially when there's a wide gulf between corporate and national cultures. After recently touring Universal Card's facility in Jacksonville, where visitors are often dazzled by the upbeat work culture, Santiago Muñoz is skeptical. Muñoz, a planning manager for Madrid-based Airtel, went through Universal Card in search of inspiration and ideas for a cellular-telephone startup in Spain. But he doubts that he could transplant Universal Card's measure-and-monitor approach to Spain, where workers are likely to rebel against a tightly controlled atmosphere. At Universal Card, employees are measured on how quickly they answer the telephones and how long they stay on the line with customers. Overhead monitors often exhort staffers to work harder and faster—things that Muñoz believes would outrage workers in his country.

Still, in many instances, these cult companies have inspired major changes. Consider Stack's open-book concept. The idea: to train employees to understand the company's finances, to share those numbers routinely with the workforce.

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and to use bonus systems and incentive pay more creatively to put some fun into meeting numerical goals. At Springfield's so-called heavy-duty plant, where workers tear down and put back together huge diesel engines, employees racked up

## Cover Story

surprise reward: leather bags for each of some 400 employees. Earlier, the plant's general manager had promised to wear a dress if the workforce could reach 500,000 accident-free hours. When they did, he slipped on a frock, and employees paraded him around the plant on a forklift.

Silly? Sure. But it put "fun" into work, transforming a serious goal into a game of sorts. And Springfield's open-book approach intrigues many companies experimenting with employee empowerment. "It's the next logical step after you've given self-directed teams the power to make decisions owners once had," says Donald L. Robb, a manager at a division of R. R. Donnelley & Sons Co., which is considering a pilot program of open-book management. "It integrates all of the other things we've been doing and gives some focus to it."

Dozens of companies, from Allstate Insurance Group to upscale sportswear maker Patagonia, have implemented Stack's "Game of Business" or portions of it. To improve a paltry 2.9% return on equity at Allstate's Business Insurance Group in South Barrington, Ill., President Jack D. Callahan eliminated layers of management and installed incentive pay plans and self-managed teams in 1991 and 1992. The changes helped, but not enough to meet Callahan's profit goals.

**NOW, A DISCIPLE.** That's when he turned to Stack's approach. The unit's 3,500 employees were trained to understand the importance of financial measures such as return on equity, and were then provided with the information on a regular basis. The result: "It got employees involved and committed, and it gave them some ownership," says Callahan. "They understood they had an impact on the bottom line." The Allstate unit's ROE hit 16.5% last year—and Callahan took early retirement to open his own consulting firm in Chicago to spread the gospel to other companies as a Stack disciple.

"Open-book" management has even spread to Zambia, where the world's fifth-largest copper mining company is using Stack's ideas to reduce costs and eke higher productivity out of its 55,000 employees. As largely uneducated workers march into the front entrance, they can't help but spot a 50-

foot-high scoreboard that lists monthly and year-to-date financials, from "copper revenue" to "corporate depreciation."

And for all the criticism of whirlwind multicompartment tours, it's often the cumulative effect of seeing the same idea enacted at several places that has real impact. After visits to General Electric, Lands' End, and Fidelity Investments, teams of managers from GTE learned that they could vastly improve service by giving employees more information and control to solve customer problems. All three outfits—widely applauded cult companies—aggressively employ technology to eliminate handoffs to other departments and employees. "After seeing what GE and Lands' End do, we were inspired to incorporate those ideas in our business," says David P. Allen,

a process team leader at GTE Telephone Operations. "The visits caused us to look for the technology that would allow a service rep to take an order without having to pass work downstream."

As a result, the average time it takes GTE to complete a customer order has fallen to less than two hours from three to four days. And the tourist has become a tour guide: Allen has hosted hundreds of outsiders who have come to GTE in the past two years to learn from his experience.

Does that sound like a frenzy that's getting out of hand? Some companies are starting to feel that way. The ever-increasing demand for visits has led more and more to close their doors. Ford, Xerox, Hewlett-Packard, and General Electric have drastically cut back on the number of sightseers they'll admit. To gain a peek at J. C. Penney Co.'s telemarketing operations in Dallas, Nynex's LeStage says he had to call a Penney manager who once coached his son's pop football team in Wilton, Conn. "The challenge in getting into some of these places is unbelievable," he says.

To keep the flood of outsiders from causing costly, time-consuming

distractions, many companies now confine visitors to formal workshops and tours, often with their own sites and staffs. The avalanche hit USAA in 1990, after the insurer gained attention for its innovative human-resource policies and customer service. By 1991, it had established a formal, day-long seminar program. "It was getting to be onerous," says Angelo de Guttadauro, who runs the program. "We just didn't have the time to devote to all these ad hoc visits."

**"A DISTRACTION."** At one point, General Electric's Answer Center in Louisville, which will handle 3.5 million telephone calls from consumers this year, was also struggling to cope with thousands of visitors from around the world. GE charged \$500 a person for a one-day seminar and tour at its



## READY, SET...

### Visitors to AT&T Universal Card's customer-service center see how employee performance is monitored

**THIS WORKER'S PHONE CALLS ARE TIMED**



Karl L. Brunson presents ideas in California from a phone modem in Manassas, Virginia.  
Which he finds much easier than hopping on planes all of the time.

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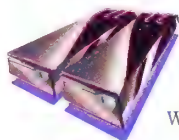
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## Cover Story



800-number customer-service center and \$4,800 for a more intensive, four-hour consulting session, a program that occupied four GE managers full-time. But now GE allows only customers and suppliers to visit—and has gotten out of the consulting business altogether. “It was becoming a distraction,” says James E. Cabral, one of the managers who ran the program for visitors. “After a while it became so burdensome, some of us couldn’t get our own jobs done.”

On the other hand, lots of companies continue to put up with all the corporate tourists and even encourage them. Universal Card may be the Disney World of management theme parks: It has hosted nearly 8,000 outsiders since 1992. Chief Executive David Hunt believes the time invested is well worth it. “We showcase AT&T’s technology here,” says Hunt. “Our suppliers better understand the need to live up to our quality standards, and we’ve developed a lot of friends who are willing to share information with us.”

**LITERARY LION.** And being the high priest of a management cult can confer extraordinary status on an executive. Johnsonville Foods’ Stayer still professes incredulity at the attention his little family-owned business receives. The interest began after Tom Peters featured Stayer and his company in a PBS special in 1987. Johnsonville was a pioneer in the use of self-managing teams to run a factory. Teammates were even given the power to hire and fire colleagues and dish out monthly incentive bonuses to one another. The changes have helped Johnsonville increase its revenues by nearly 20% a year for the past decade. “After the show, they all wanted to come and talk and see,” Stayer recalls. Multitudes of managers from such corporate heavyweights as Campbell Soup and Ford descended on the company.

## PRESSING BUSINESS

### USAA’s innovative efforts to keep employees happy draw an avalanche of visitors

**SPORTS FACILITIES ARE EXPANSIVE**

Things really took off after Stayer wrote an article entitled “How I Learned to Let My Workers Lead” for the *Harvard Business Review* in late 1990. “It was like an explosion,” he says. So many people wanted to visit in 1991 that Stayer launched the company’s one-day seminar, featuring candid chats with five Johnsonville “members” and a bratwurst picnic lunch for \$235 a person. Stayer now spends most of his time consulting with such companies as Frito-Lay, B.M. McDonnell Douglas, and Brownrigg Ferris. He contends his absence hasn’t hurt his colleagues back at the office because he has delegated authority to three key teams. “I’m not in charge of doing,” Stayer says. “I’m in charge of leadership, of stirring the pot, of coaching.”

Many of his visitors have brought back to their own facilities the stories behind Johnsonville’s move toward self-managing teams, hoping to learn from Stayer’s successes and mistakes. Yet even Stayer has misgivings about the worship Johnsonville inspires. “I’ve always been concerned that people were making us a lot better than we are,” he says. “Johnsonville is a heck a lot better than it used to be, but coming here is not going to solve all a manager’s problems. If you don’t produce results for customers, you don’t stay in business.”

Amen. Modern managers are wise to learn from other companies willing to share their ideas, but they can’t forget that the tours in the world aren’t going to give them the competitive edge they need to survive and thrive. It still comes down to the obvious: Produce a product people want at a competitive price and you will succeed. Simple as that idea may be, however, the path to true enlightenment is never easy.

*By John A. Byrne in New York*

CONTINUED ON PAGE 134

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# IT'S NOT EASY MAKING PIXIE DUST

**W**e are in the Utilidor—a series of tunnels below Disney World's Magic Kingdom theme park in Orlando. The tunnel complex is generally off-limits to outsiders, but not to 41 visiting managers whose companies have anted up \$2,295 a head so they can learn about Walt Disney Co.'s ap-

## Cover Story

proach to people management.

This underground city is a beehive of activity. Employees rush through the gray concrete tunnels, scrambling to put on costumes and assume their roles upstairs. Golf carts speed by with supplies. Makeup artists prepare an array of Cinderella and Snow White wigs.

Before coming to this 3½-day seminar, I was skeptical. The program sounded like little more than a dream junket: three nights at the resort's most elegant hotel, plus four-day passes to Disney's theme parks. Besides, I thought, what could any manager possibly learn at Disney World? By the end of the first day's activities, however, my note pad was brimming with ideas and lessons dished out by Disney staff.

My colleagues, most of them human-resource managers, take the program seriously. Most are facing a slew of challenges in need of Disney-style magic. A delivery manager at Anheuser-Busch Cos. is trying to make his drivers more responsive to retailers. Personnel managers at a fast-growing bagel chain in Florida worry about maintaining standards as they beef up the chain's ranks. And an employee trainer at South Africa's state-owned transportation conglomerate is looking for ways to streamline the company's hiring process.

**BLUNT FILM.** Disney's reputation for cleanliness, attention to detail, and helpful employees is what has drawn them here. "Everyone knows how wonderful Disney is, so you figure they must be doing something right," says Kathleen Scappini, who works for SNET Multi-Media in West Hartford, Conn. That "something right" is

what Disney refers to as the "pixie-dust" formula, with four key ingredients—employee selection, training, support, and benefits. Our seminar, "Disney's Approach to People Management," promises to reveal how the company motivates employees.

Instructors, called facilitators, tell us that we cannot count on Tinkerbell. "The solutions are not complicated," assures Jeff Soluri, a Disney instructor. "It's attention to detail and hard-nosed business practices that produce the magic."

If there is pixie dust, it starts with the hiring process. One of the first activities is a field trip to Disney's "casting center," a Venetian-style castle where job candidates view a video before being interviewed. The short film informs job seekers about the company's strict

sure. To do so, the company tells its cast, is to risk alienating a guest, spoiling the illusion, and damaging Disney's standing in entertainment and American culture.

**A BIT OF GROUSING.** Between excursions, participants share what they have learned—and what they might use. Disney staffers with wireless microphones dart Oprah-like through a conference room seeking comments. They get plenty. John Lealos, the Anheuser-Busch manager, says he wants to incorporate more of an appreciative, team feel into his unit's corporate culture. "If we can get that kind of atmosphere at our company, the productivity will go up," he says. Hugo Strydom, the training manager at South Africa's Transmit Ltd., intends to use a Disney-style orientation to weed out weak candi-



appearance guidelines (one ring per hand and no tattoos, please) and the rigors of the work. By being blunt and detailed, Disney says, it's able to weed out incompatible candidates at the first crack.

The critical part of the process, though, is employee training. New hires, who average less than \$10 an hour, are treated to a visual company history. They are told that they are not just employees but pivotal "cast members" in a "show." From street sweepers to monorail pilots, each cast member must go out of his way to make the resort seem unreal. No matter how tired workers are or how deeply guests may try their patience, they must never lose compo-

**LEARNING HOW TO  
MAKE EMPLOYEES  
PART OF THE SHOW**

dates in a major hiring blitz.

Not everyone is happy.

Some managers privately say they're disappointed that the Disney magic was, well, not really magical at all. They complain that the program covered only operations in Orlando and not Disney's global activities. Others find the ideas being preached not all that original. "We're already doing many of the same things," grouses one manager.

Maybe. But I brought back enough ideas to give my bureau manager a raft of suggestions to implement in Miami. They aren't earth-shattering proposals—but I'm not Tinkerbell, either.

*By Antonio Fins in Orlando*

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LIFE INSURANCE

# MIDLIFE CRISIS FOR INSURERS

In a mature market, the way to grab share is to grab rivals

The pace of change in the life-insurance industry, where product cycles sometimes seem to span decades, has tended to range from glacial. Life insurers have been relatively small players in the gale-force merger activity that has buffeted most Corporate America for the past couple of years.

Nowadays, however, the chief executive of an underperforming life insurance company is well advised to scratch his back as well as his chest. Merger mania has been hitting life insurers hard. Already this year, the volume of deals, at \$7.5 billion, far surpasses the total for all of 1994 (chart, page 138). Among the biggest: Metropolitan Life

and New England Life, Jefferson-Pilot and Alexander Hamilton, Humana and Emphesys Financial Group. "If we now have 100 to 200 significant life insurers," says Michael W. Blumstein, an insurance analyst at Morgan Stanley & Co., "five years from now it could be down by a third."

Why the Urge to Merge?

**COMPETITION** With banks and mutual-fund companies grabbing share in the market for annuities, insurance companies have to get their costs down to stay in the game. Mergers allow insurers to achieve greater economies of scale.

**SLOW GROWTH** Life insurance is a mature industry. Acquisitions are the easiest route to expanding market share.

Like the wave of banking mergers, the insurance consolidation has the potential to make a lumbering, fragmented industry vastly more efficient by forcing companies to squeeze out costs and modernize operating systems. Even mutual insurers, many of which have been particularly slow to modernize, are getting in on the action. But the consolidation could be disruptive for consumers and disastrous for the 200,000 or so agents who today represent the primary—and very costly—means of selling policies. Says David S. Kimmel, a vice-president in the insurance advisory group at J. P.

Morgan & Co.: "Insurance companies are going to have to dramatically reduce distribution costs, and I think the real losers are the agents."

**HIGH COSTS.** Several forces are coming together to force the consolidation. For starters, with the population growing only slowly and the competition for consumer savings increasingly fierce, "life insurance in the U.S. is a very mature market," says James R. Tuerrf, president of American General Corp. That means the best way for companies to grab market share is to grab each other, as even such mutuals as Massachusetts Mutual Life Insurance Co. and Connecticut Mutual Life Insurance Co. are now contemplating. "The product's essentially a commodity," says Ron W. Frank, senior insurance analyst at Smith Barney Inc. "The competitive edge comes from [lower] expenses and distribution. Those point

**RATINGS** Insurance rating agencies are coming down harder on mutual companies low in capital. Mergers offer an easy route to higher ratings, important to winning agents' and consumers' confidence.

**TECHNOLOGY** Technology is fast becoming a key competitive edge. Mergers permit greater investment to modernize back-office and distribution systems.



# Insurers will have to "dramatically reduce costs, and I think the real losers are the agents"

you in the direction of consolidation."

Cost pressures are a factor as well, thanks in large part to life insurers' reliance on agents. Moody's Investors Service says new business production costs can actually exceed insurers' expected revenues. Larry G. Mayewski, a senior vice-president at A. M. Best Co., says that although costs have dropped, commissions and other compensation still account for some 54% of life insurers' first-year direct premiums.

Insurers also face intensifying competition in the rapidly growing markets for such products as annuities and mutual funds. The annuity business is expanding rapidly, but close to 18% of annuities are sold through banks, which are gaining market share. Fidelity Investments and other brokerage houses also are pushing annuities, and insurers face just as many rivals selling mutual funds.

**RAPID CHANGE.** Then there are regulatory pressures. Many insurers, particularly mutuals, are somewhat low on capital under the new risk-based standards. That's hurting them with rating agencies, and that in turn makes it harder for them to deal with agents and consumers wary of low-rated insurance companies. For their part, health insurers, whether independent or affiliated with life companies, are contending with rapid change on both the competitive and the regulatory fronts. Many among them are merging simply to build competitive clout.

As if these pressures weren't enough, changing technology is adding to the drive for consolidation. Consumers are getting more of their financial needs met electronically, and life-insurance companies have begun to realize that they may have to follow suit with some products. Growing numbers also realize that they need to bulk up to be able to afford to modernize their back offices and get their costs more in line with nonbank competitors. "A lot of these companies are small," says Gary C. Wendt, chief executive of GE Capital Services Inc., which has spent more than \$1.5 billion in the past two years snapping up life and health insurers. "They don't have enough scale to power into these [new] markets."

The drive for clout and technological prowess were key factors for Harry P. Kamen, chairman and CEO of Metropolitan Life Insurance Co., when he agreed to a \$2 billion deal with New England Mutual Life Insurance Co., whose presence with affluent customers complements MetLife's prowess with middle-income consumers. "The market we were not comfortable in was the market New England was strong in," he says. "We would have [had] to spend more in computers and so on, and we still wanted to put money in our core middle-market [business]. This comes with ready-built systems."

Kamen says that agents will benefit

insurance industry will go through the same changes the brokerage business did in the 1970s, when commissions were deregulated. Today, he says, only a third of all brokerage customers deal with full-service registered representatives—not exactly a rosy prospect for full-service agents.

**FRUSTRATION.** Consumers, though, could ultimately benefit from the merger. Robert Hunter, director of insurance for the Consumer Federation of America, says that as high-cost, high-price players are forced into the arms of more efficient companies, consumers will be better served. Another plus: Consumers holding policies from weak companies

could have them taken over by stronger insurers. But as their policies change hands and the inevitable mishaps crop up, consumers could be frustrated.

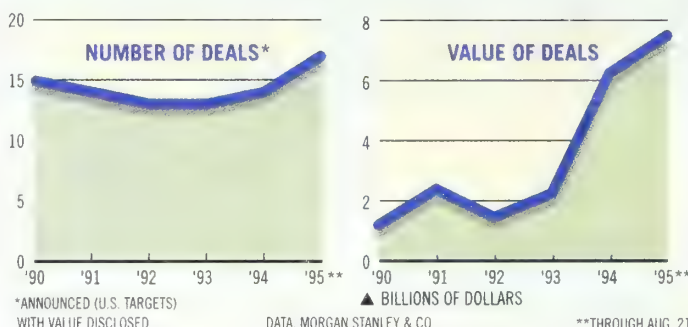
Who's the next merger bait? Potentially, almost anyone. Gary W. Parr, head of the insurance group at Morgan Stanley & Co., sees intense merger activity for the foreseeable future. "We've got a lot of business in the backlog, and we're working on a lot of strategic

assignments" involving insurers, Parr says.

That's good news for Morgan Stanley and for farsighted insurers. But woe for the companies that are simply trying to be big. Banks that have grown too large and diffuse have come under attack from shareholders. And insurers that embrace size for its own sake run the same risk. Industry experts say big, faltering multiline insurers, such as Aetna Life & Casualty Co., are warnings to insurers that are trying to expand too fast. "By the year 2000, the multiline insurance company as we know it in the U.S. will not exist," says David W. Nelson, managing director and global insurance executive at Chase Manhattan Corp. "The expense bases of these companies are too large, and the businesses have been unfocused for too long." Size counts for a lot in insurance. But it's not a cure-all. All the consolidation in the world will not make life insurance a growth product again.

By Kelley Holland in New York and Tim Smart in Hartford

## GETTING IT TOGETHER



from all the mergers taking place. "Industrywide, every transaction that strengthens a company helps the agent," he says, because agents have an easier time selling the products of a strong company. But others beg to differ. The average agent today sells just one policy per week. That is a grossly inefficient sales process for mass marketing when the average life-insurance policy sells for just \$750, according to Robert S. Morette, a vice-president at Boston Consulting Group Inc. Robert W. Fiondella, president and chairman of Phoenix Home Life Mutual Insurance Co., charging that the agency system "is doing a lousy job" for the industry, is reducing the proportion of his business that depends on agents by expanding his company's presence in the mutual-fund market through a deal with Duff & Phelps.

Some believe the cost pressures driving consolidation will lead to a fundamental shift away from the agency system altogether. Richard K. Berry, managing principal at the consulting firm Towers Perrin, predicts that the

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# THIS ANTITHEFT COMPANY IS FEELING INSECURE

Sensormatic's accounting is being probed as the shorts take aim

**T**his should have been a banner year for Ronald G. Assaf. Nearly 30 years after he co-founded Sensormatic Electronics Corp., the maker of antitheft and security devices appeared to be hitting its stride. Revenues of the company, based in Deerfield Beach, Fla., have grown at a 40% annual clip over the past three years and were expected to hit an estimated \$920 million for the

credibility, and countering contentions that Sensormatic's products cause problems with pacemakers. In March, he was jolted by the unexpected resignation, for personal reasons, of Michael E. Pardue, who served as chief operating officer, chief financial officer, and liaison with Wall Street. Assaf admits the company's controls and systems have been inadequate. On July 7, Sensormat-

Corp., the European rival, were properly expensed. The company says it doesn't believe there will be any "major write-offs."

Wall Street short-sellers, who thrive on signs of accounting shenanigans, have targeted the company. While that pressure on the stock, it was the July announcement that caused the stock to fall to 23 from a high of 36 two days earlier. On Sept. 6, it was selling at 20.

Sensormatic primarily makes anti-theft devices that foil employment theft and shoplifting, especially the familiar white plastic "alligator" tags on apparel. In recent years, it has diversified into antitheft systems for "hazardous goods," such as power drills and sunglasses, and security systems for commercial and industrial clients.

**"EARLY WARNING SIGN."** The short-sellers point out that while Sensormatic dominates the market, it faces growing competition, especially from rival Checkpoint Systems Inc. And they contend—while Assaf denies—that Sensormatic's electromagnetic systems interfere with the functioning of pacemakers. The Food and Drug Administration is exploring the effect of electronic article surveillance on pacemakers and similar devices.

But on Wall Street, it's the accounting issues that reverberate. While Sensormatic is a manufacturer, its balance sheet makes it a finance company in sorts. Sensormatic leases systems and offers favorable financing to buyers. Historically, it has carried a hefty accounts-receivable balance. To maintain cash flow, it sells financial portions of the

counts receivable, as well as leases, with full or partial recourse to the company. But recently, its accounting for revenues from deferred sales and sales-type leases has caught the attention of critics. Howard M. Schilit, an accounting professor at American University and president of the independent Center for Financial Research & Analysis, commented in a December report that Sensormatic's revenue accounting, while permissible under generally accepted accounting

## SENSORMATIC'S WILD RIDE

**1968** Ronald Assaf co-founds Sensormatic Electronics, which becomes top provider of antitheft devices to retailers. Company chalks up fairly consistent revenue and earnings gains.

**DECEMBER, 1994** Company's accounting practices come under review by Center for Financial Research & Analysis, which terms them "aggressive." Short-sellers begin targeting the stock, citing other accounting issues. Company defends its accounting practices. Stock begins falling.

**MARCH, 1995** Michael Pardue, COO and CFO, announces his resignation, which shocks analysts.

**JULY 7** Announces earnings won't meet analysts' projections for fourth quarter and full year, blaming shortfall in anticipated revenue and higher expenses from European acquisition. Stock drops 35%. Shareholders file lawsuits.

**AUG. 31** Announces that 1995 results will be delayed pending an extended audit expected to be completed by mid-September.

DATA BUSINESS WEEK



**ASSAF ADMITS GROWTH LIKELY GOT AHEAD OF CONTROLS**

year ended June 30. In January, it completed the acquisition of a major competitor's operations in Europe. And Sensormatic is gearing up for a high-profile role as a sponsor and the provider of electronic security systems for the 1996 Olympics in Atlanta.

Instead, Assaf finds himself defending the company's accounting practices and business prospects, shoring up damaged

reputation. He said earnings would be substantially below expectations and below last year's fourth quarter.

Most troublesome was an Aug. 31 announcement that release of 1995 results would be delayed, pending an extended audit by Ernst & Young that is to be completed by mid-September. The audit is examining whether revenue was properly booked before products were shipped and whether costs associated with the merger with Knogo

counts receivable, as well as leases, with full or partial recourse to the company.

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principles, was "overly aggressive." Sensormatic records revenues at the time of sale, rather than when payments are substantially received.

The resulting shortfall from the gap between net income and cash flow from operations, Schilit says, is problematic. In the nine months ended Mar. 31, for example, the company had net income of \$69 million and a negative operating cash flow of \$50 million. Bank borrowings rose to \$122 million, from \$6.7 million during the same period in 1994. "I know of no better early warning sign of a company in trouble than one whose cash flow from operations is significantly less than net income over a period of time," he says.

The company has also come under fire from short-sellers and a shareholder lawsuit filed on Aug. 3 against the company and Ernst & Young for other accounting practices. The suit, claiming violations of securities laws, contends the company lowered its reserves for doubtful accounts even while its revenues and receivables were increasing. For the quarter ended Mar. 31, the suit notes, revenues increased 47% over the comparable earlier period, but Sensormatic's allowance for doubtful accounts as a percentage of gross receivables dropped to 3.9% from 4.9%. That, in turn, buoys earnings. "If they had not reduced their reserves, chances are they would not have made the Wall Street estimates," says short-seller Bart Blout.

**CREDIBILITY ISSUE.** Assaf denies the suit's allegations and claims that the company has never had a problem with bad accounts. With large retailers such as Wal-Mart Stores Inc. and Kmart Corp. as clients, he says, the reserve ratio could be reduced. While both inventory levels and bank debt are higher than he would like, Assaf insists the company is financially sound and is projecting positive cash flow in 1996. The company's accounting policies have been consistent, he claims, and the extended audit has nothing to do with the issues raised by short-sellers. "They've been attacking our accounting for a year, and there's nothing wrong with our accounting," he says.

Assaf, though, doesn't dispute Paine-Webber Inc. analyst Steven M. Fortuna's view that, considering the earnings shortfall and audit problems, "management's credibility is at issue." Says Assaf: "Our growth has probably outpaced our systems and management controls, and we have a challenge here." So do Sensormatic's shareholders.

*By Gail DeGeorge in Miami, Fla.*

## SECURITIES FIRMS

# LOOKS LIKE AFFIRMATIVE INACTION

Some minority firms are angry at an Oppenheimer Capital play

**W**all Street brokerage houses, never known as bastions of diversity, are under growing pressure to do business with firms owned by minorities and women. The California Public Employees' Retirement System (CalPERS), which manages \$90 billion in pension funds, encourages its money managers to ensure that 15% of their trades are executed by minority-owned firms, 5% by women-owned firms, and 2% to 3% by disabled veteran-owned firms. But these efforts can backfire. Case in point: Oppenheimer Capital, which manages \$32 billion, has enraged some minority- and women-owned brokerage firms.

The controversy began last March when Oppenheimer Capital invited minority- and women-owned firms to apply to do business with it. A Mar. 9 letter to prospective firms obliquely described the arrangement: Oppenheimer Capital would send a portion of its brokerage business to Emmett A. Larkin Co., an Asian-owned firm in San Francisco. Larkin would execute and clear all the trades, then forward a portion of the commissions to the other firms, which would have nothing to do with the orders. As the letter put it, "Larkin will then send commission checks to your firm as designated by Oppenheimer Capital." Says an irate Leopoldo E. Guzman, who heads Miami-based Guzman & Co.: "It is a handout. They've set up a little hot-soup window and said, 'Don't mix with the real broker-dealers.'" Larkin didn't return calls.

Why would Oppenheimer do this? The sister company of Oppenheimer & Co., the large Wall Street brokerage firm, declined comment. But sources

close to the firm provide this rationale: It wanted to be able to represent accurately to its public clients that it had paid minority firms. At the same time, say the sources, Oppenheimer Capital believes that its main obligation is to its clients, and that a number of the small firms seeking business don't reliably answer their phones during business hours, much less have the experience to execute large trades. Further, Oppenheimer expects to receive research from the nine minority- and women-owned firms it recently selected; these include WR Lard & Co. in New York, which declined comment, and HCM Investments Inc. in Chicago, which says it believes that it will be executing trades for Oppenheimer and providing research.

**NO PROBLEM.** Guzman and executives at several women-owned firms, including Muriel Siebert & Co. in New York and Western Select Securities Inc. in San Francisco, are outraged. They want a chance to prove themselves by

## HELPING OR HURTING?

*How Oppenheimer does business with minority firms*

- Oppenheimer Capital selects nine minority- and women-owned firms to handle a portion of its brokerage business.
- But instead of apportioning the business among all nine firms, it sends all the trades to just one firm, Emmett A. Larkin Co., which executes and clears the orders.
- Oppenheimer directs Larkin simply to send commission checks to the other firms, though they have no involvement with the trades. Sources say Oppenheimer feels small firms lack sufficient expertise to handle the trading business.

DATA: BUSINESS WEEK

executing trades for big clients. There are other money managers that have programs employing small firms to execute trades. For example, Boston-based State Street Global Advisors, with \$1 billion in equity portfolios, chose 80 minority- and women-owned broker-dealers that they do business with, plus 80 to 100 other firms. Chris Hyne, managing director at State Street, says money managers tend to see the rule about using minority-owned firms as a problem, but "we looked at it like an opportunity." Oppenheimer's use of minority firms, unfortunately, could well become a liability.

*By Leah Nathans Spiro in New York*

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# ARIS DOESN'T FIT SARA LEE LIKE A GLOVE ANYMORE

Management blunders have plagued the accessories unit

**W**hen former Aris Isotoner Inc. Vice-President Richard Rubin testified at the O.J. Simpson trial in June that the bloody glove found at the murder scene could well have shrunk by as much as 15%, it didn't occur to him that the extra-large Aris Lite could be a reasonable metaphor for the company he left five years earlier.

Back in 1990, when O.J.'s wife, Nicole, whom he is charged with slaying, bought him a pair of Aris gloves at Bloomingdale's, the Sara Lee Corp. unit was rapidly growing and highly profitable, the envy of the U.S. accessories industry.

Although Aris is still the nation's largest glovemaker, with a dress glove market share estimated at more than 60%, it has, according to people familiar with the company, fallen victim lately to a series of snafus that have damaged its ties with retailers and eroded sales and profitability. After sending in two new CEOs in as many years with orders to boost profits, Sara Lee, which bought Aris in 1969 in one of its first nonfood acquisitions, has dramatically scaled back Aris' operations. On Sept. 4, the giant Chicago-based consumer-goods concern began notifying about 7,000 full-time workers at Aris' huge glovemaking plant in Manila that it would shut the facility and eliminate their jobs to shift production to countries where labor is even cheaper.

**THE SETUP.** The company doesn't publicly report financial results for Aris Isotoner or other subsidiaries. Nor do analysts follow Aris closely, because its contribution to Sara Lee's \$17.7 billion in annual sales is relatively minuscule. But former Aris executives say the 86-year-old company posted an operating loss on an esti-



## OUT OF HAND?

Former Aris Chairman Lari Stanton (above) was forced out in a 1993 purge of senior executives. Since then, sources say, the maker of the infamous "bloody glove" has faltered

estimated \$185 million in sales in the fiscal year ended June 30—a far cry from the estimated \$35 million in operating income on \$230 million in sales they say it delivered to Sara Lee in fiscal 1993.

To be sure, Aris Isotoner's revenues were hurt by an unusually mild winter, the ongoing consolidation of traditional department stores, and lower prices demanded by discount retailers.

But by most accounts, Sara Lee set Aris up for trouble in 1993, when Lew Frankfort, the newly appointed head of Sara Lee's accessories division, forced the retirements of Chairman and COO Lari Stanton, a popular and well-



regarded executive, and other senior officers. Frankfort replaced Stanton, 67, with David W. Bryan, 49 [no relation to Sara Lee CEO John H. Bryan], who had earned his stripes in Sara Lee's bakery unit marketing such brands as Sara Lee cheesecake and bagels. Frankfort, says an embittered Stanton, no senior vice-president at second-ranked glovemaker Fownes Brothers & Co. "decimated the whole management team." In a bid to double sales, to \$50 million, in five years, Sara Lee replaced veteran executives with people who lacked their experience in the glove industries. Says Stanton, the grandson of Aris founder Adolph Steinberger, "Bryan tried to run a glove company like a bakery."

**NEW SYSTEMS.** Indeed, Bryan and his associates quickly discovered that leather goods and cheesecake are different worlds. For one thing, they found that tampering with a well-oiled sales, production, and distribution apparatus can be disastrous in a quirky business in which lead times for ordering skins exceed six months and most sales occur between Thanksgiving and Christmas. Says R. Schroder, who recently retired as president of Aris (Philippines) Inc.: "They came in completely unfamiliar with the company and tried to install new systems...and change everything." Wor-

complaints Harry H. Albritton, former vice-president for sales, says Bryan "tended to avoid talking to customers."

Bryan, who left Aris in September, 1994, and is now president of cycling gear maker Avedis Zilejian Co., declined comment on his performance at Aris or the reasons for leaving. Frankfort is now CEO of Sara Lee's Champion Intimates, and Accessories operations but is no longer responsible for Aris. He could be reached for comment.

Jack W. Salisbury Jr., a former senior vice-president with Sara Lee's Playtex Apparel Inc. unit who succeeded Bryan as president and CEO of Aris in September, 1994, called last year's single-digit sales drop "disappointing" and blamed it on the weather and late deliveries and nondeliveries. Aris, he says, is now pinning its hopes for a rebound on a cold winter, new glove styles, and an expanded casual-footwear line. Meanwhile, he says, Aris doesn't plan to capitalize on its notoriety. But it certainly can't hurt.

By Phillip L. Zweig in New York

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BY GENE G. MARCIAL

## FIRST INTERSTATE: UP FOR GRABS?

Investors who took George Salem's advice last month certainly made a bundle. He sent clients an alert on Aug. 9 to snap up shares of Chemical Banking and Chase Manhattan in anticipation of a "potential merger." Events bore him out on Aug. 28, when the announcement drove up shares sharply. Salem, senior-vice president at New York investment firm Gerard Klauer Mattison, is now high on another bank: First Interstate Bancorp (1).

Why? Salem thinks this Los Angeles bank, now at 96 a share, will be acquired by San Francisco's Wells Fargo at about 120. "First Interstate has become the most attractive target in the industry," argues Salem, who says the two need each other to maintain competitiveness, boost earnings, and roll back costs.

First Interstate, with 1,137 retail branches in 13 Western states—mainly California, Texas, and Washington—is an alluring target for other banks, too: NationsBank, Banc One, and Norwest, says Salem. But he reckons Wells Fargo will be the one to snare First Interstate: Wells Fargo's position would suf-

book value. First Interstate, with assets of \$56 billion, trades at 187% of book.

A buyout of First Interstate at 120 a share may appear pricey, concedes Salem. But he says such a deal would push up Wells's 1997 earnings "by at least 10% at the outset."

Wells Fargo Chairman Carl Reichardt has been after First Interstate since 1992, says Salem. But Interstate's then-CEO, Ed Carson, was unwilling to sell until the turnaround he had been orchestrating was complete. Now, "management can collect full value for its hard work," notes Salem.

Both banks have relatively new CEOs—Bill Siart at Interstate and Paul Hazen at Wells. Salem believes they are more willing to negotiate a merger in light of the recent wave of consolidation. All major bank holding companies "are now considering merger alternatives that had not been in their plans a few months ago," asserts Salem. Spokespersons for Interstate and Wells Fargo declined comment.



**SEER SALEM:** The Chase-Chemical deal was no shock

and CEO Steven Georgiev expects FDA clearance by early 1996.

Each year, about 1 million women remove unwanted hair through electrolysis, a painful process. Lasers are less painful, quicker, and less expensive, according to Thermolase and Palomar. Palomar already has the manufacturing capacity and distribution system to market its product, says Georgiev. Palomar's Spectrum Medical Technologies division markets a laser system to remove tattoos, birthmarks and other skin lesions.

Palomar, which expects to post a 60¢-a-share loss this year, should make 39¢ in 1996, on estimated sales of \$2 million, vs. a 1994 loss of \$1.31 a share on sales of \$14.6 million, estimates Amy Bell, an analyst at H.J. Myers. Based on this outlook, the stock should hit 10 this year, figures one big investor.

## ORNDA IS ON THE EXAMINING TABLE

Don't count hospitals out of the current mergers-and-acquisitions race. Hospital-management stocks have been in full recovery this year, and the biggies in the group—Columbia/HCA, Healthcare and Tenet Healthcare—have been on the prowl. The third largest publicly traded hospital-management company, OrNda (ORND), pronounced Orinda, will likely be the next target of either Columbia/HCA or Tenet. So say some buyout pros who have been buying into OrNda, which provides inpatient and outpatient services at its 47 hospitals in 14 states.

OrNda stock had been on the rise—from 15¢ in early June to 21 on Sept. 5—partly because of prospects of a buyout, says a New York money manager. He says Columbia/HCA and Tenet are interested in OrNda's networks in Arizona, Southern California, South eastern Florida, Texas, and Nevada.

OrNda "has the best operating management in the industry," says one investment banker, who finds it "the most undervalued—and still underappreciated stock in the group." In a buyout, he puts OrNda's worth at 30.

He notes that the company has been growing fast, mainly through acquisitions, since emerging from bankruptcy proceedings in 1990. Analysts see OrNda making \$1.50 a share this year and \$1.75 next, vs. a loss of \$1.29 last year. OrNda officials weren't available for comment.

## WELLS FARGO MAY BE CALLING



fer if somebody else got it. "Wells Fargo has a strong geographical fit with First Interstate," he says.

Wells is the 15th-largest U.S. bank holding company and the owner of California's second-largest bank. But with a one-state market and assets of only \$50 billion, "it may not be large enough to be competitive in the emerging banking world," Salem says. With its stock at 186 and market cap of \$9 billion, Wells Fargo is trading at a lofty 261% of its

## ZAPPING HAIR MAY GIVE PALOMAR ZIP

Starting in mid-August, Palomar Medical Technologies (PMTI) stock took a leap: from 2¢ to more than 4¢ by the end of the month. And it may be headed higher still.

The reason: Palomar will soon announce a licensing pact to market Massachusetts General Hospital's technology for laser-based hair removal. Palomar would thus compete head-on with Thermolase, whose stock has soared from 4 to 24 this year because of its laser technology that removes unwanted hair follicles. Some of those buying Palomar in mid-August were Thermolase investors who learned of Palomar's entry into the \$1 billion hair-removal market.

The agreement gives Palomar access to Mass General's clinical data, which show the safety and efficacy of its system and will let Palomar file for FDA approval of the system, whose patent is still pending. Palomar Chairman

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## LAWSUITS

# LOOK WHO'S FEEDING THE LITIGATION FIRE

The Chamber of Commerce, tort-reform lover, is filing lawsuits

No sooner had President Clinton announced an executive order banning striker replacements for federal contractors last March than Stephen A. Bokart got an urgent call from lawyers for Bridgestone/Firestone Inc. The attorneys for the tiremaker, then in the midst of a bitter strike, wanted to know if Bokart, general counsel of the U.S. Chamber of Commerce, would file a suit challenging the executive order.

For Bokart, the decision was easy. He had just finished meeting with outraged business lobbyists who had defeated a striker-replacement ban in Congress. "The issue was tailor-made for us," he says. "Everyone thought it was a cheap shot from the President." Within a week, the chamber had filed a lawsuit seeking to block Clinton's order.

**TAKING ON NADER.** What a turnaround: The very trade association of Corporate America that for years has sought tort reform to keep claimants out of the courtroom is now lobbying lawsuits in record numbers. Content during the Reagan and Bush eras to file friend-of-the-court briefs from the sidelines to bolster members' lawsuits, chamber lawyers have been roused to action by the Clinton Administration. The group's recent litigation is a "response to the President's regulatory agenda," explains Bokart. "Who's sitting in the White House is a primary motivator."

The National Chamber Litigation Center was founded in 1977 as a response to the public-interest litigation groups formed years earlier by Ralph Nader's consumer advocates. But its voice hasn't been a loud one. With an annual budget of roughly \$500,000, the chamber's three-lawyer team has filed only about 25 lawsuits—mostly Carter Administration-era battles against worker-safety and workplace-discrimination regulations—and 120 friend-of-the-court briefs in those 18 years.

But lately, the pace is quickening. The chamber has five pending lawsuits challenging labor and environmental rules at the state and federal levels, a record case load. A July 31 federal court ruling on the chamber's striker-replacement suit upheld Clinton's order, but blocked its implementation because it could rob companies of a key lever in collective bargaining negotiations. The chamber has since filed an appeal challenging the legality of the President's ban. But it faces an uphill battle, since courts generally give the Oval Office wide leeway in issuing executive orders.

In addition, the chamber and other groups early this year asked a federal appeals court in Washington to declare an Interior Dept. Superfund rule overly punitive. And teaming up with other groups, it forced a settlement requiring the Environmental Protection Agency to issue less-intrusive hazardous-waste rules by December.

The chamber even scored a recent win against its other nemesis: the state of California. On Aug. 24, the federal appeals court in San Francisco struck down a Contra Costa County ordinance requiring employers to pay county-set wages on private construction projects. The court agreed with chamber lawyers that mandating government-imposed wage rates violates the collective-bargaining rights of private em-

ployers and workers under the National Labor Relations Act.

Meanwhile, the chamber and other trade groups are fighting California's green-marketing statute. The law imposes advertising restrictions on companies claiming their products are environmentally safe or recyclable. But opponents say the rules are so broad-written they often prevent information beyond the most basic statements, such as Del Monte ads explaining the recycling virtues of tin cans. In July, the chamber asked the U.S. Supreme Court to decide whether the restrictions trample on commercial-speech rights.

**CRUSADERS.** Private companies seek to challenge the chamber's imprimatur to give seeming parochial complaints greater weight and in some cases, to find political cover. "We picked the chamber because it's a broad-based organization," says David Groninger, general counsel at Nashville-based Bridgestone/Firestone. The striker-replacement ban "impacts a lot of industries besides ours." But labor contends that the chamber does little to help companies advance their cause. "They're just another voice without much more to say," says one lawyer involved in the striker-replacement case.

"Management already has top-drawer lawyers and doesn't need outside legal help."

Nonetheless, the corporate community likes their trade group's new crusading style. The chamber has "some of the finest lawyers that remember their oath to protect everybody's rights," says William A. Stone, chief executive of Kentucky-based Louisville Plate Glass Co., a nonunion shop that once used striker replacements. As long as there's pro-regulation President in the White House, Bokart's lawyers will keep the guns aimed at ready.

By Catherine Yarnall  
in Washington



The chamber has challenged labor rules, including a suit against Clinton's striker-replacement ban



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## MINORITIES

# BLACKS VOTING REPUBLICAN? IF JACK KEMP HAS HIS WAY

He's pushing a minority-friendly agenda in Congress

**J**ack Kemp isn't running for anything. Except, perhaps, Matchmaker of the Year. The former Housing & Urban Development Secretary is attempting to arrange a marriage between black voters and Republicans at the unlikely altar of affirmative action. At stake, Kemp believes, is nothing less than the future of the GOP and the health of America's inner cities.

Certainly, today's headlines don't point to any romance between African Americans and the GOP. The three leading Republican Presidential candidates are all vowing an end to minority set-asides, hiring quotas, and racially based college admissions.

**"MEND IT."** But in Congress, it's another story, due in large part to Kemp's prodding and the support of House Speaker Newt Gingrich (R-Ga.). Worried that a sharp reversal of racial set-asides will harm the party's efforts to recruit black voters in 1996, Senate and House Republicans are scrambling to come up with a minority-friendly alternative. Preparing for the post-recess legislative blitz, Republicans are writing bills featuring big tax breaks for companies and individuals willing to invest in inner cities. The legislation will be billed as the GOP's counterpoint to the "mend it, don't end it"

White House approach to the federal government's 160 affirmative action programs. Meanwhile, some Republican congressmen are readying a heavyweight lobbying campaign to close the deal.

The Republican package is the brainchild of Kemp, who never misses a chance to celebrate the GOP as the "party of Lincoln." Says Kemp: "Affirmative action has to be replaced by something. Otherwise, we just signal millions

of Americans of color that there's no place in the party for them."

The appeal has worked with younger party members. In the Senate, Republicans led by freshman Spencer Abraham (R-Mich.) will wrap some new ideas around a bundle of GOP policy perennials. The result: 100 "enhanced enterprise zones" that would enjoy big tax cuts, reduced regulation, federal help in home buying, and school vouchers. Current tax breaks targeted at inner cities



**SOLUTION 1** Affirmative action has to be replaced by something. Otherwise, we just signal millions of Americans of color that there's no place in the party for them — JACK KEMP

are considered too weak to be effective.

Under the most generous of the proposals, taxpayers could deduct the cost of buying up to \$500,000 worth of stock in a company located within a zone. Then, if the stock is held for five years, any profits on the sale would be exempt from federal capital-gains taxes. Businesses within the zone could deduct twice their usual limits for new plant and equipment. Tax credits would

offset some construction costs. And federal regulatory agencies could be asked to grant waivers to the projects as long as health and safety are not affected.

The biggest hurdle could be the package's 5-year, \$7 billion price tag. Y. Kemp argues that the plan would boost the economy of many cities, cut chronic unemployment, and bolster party strength. "With this kind of approach, third to 40% of the minority vote could go to Republicans," he says with his typical put-me-in, coach optimism.

Gingrich insists that a package of inner-city development incentives is vital to the resurgence of Republicanism that will appeal to minorities. He promised members to "focus more of our energy on how we can sign a helping hand" and has asked Representative J. C. Watts Jr. (R-Okla.), one of only two black House GOP members, to draft an alternative to racial preferences. Watts is focusing on school choice and capital formation as the key to developing

the inner cities. Bankruptcy laws and institutions lending money within an enterprise zone would be exempt from the usual paperwork requirements of the Community Reinvestment Act. A portion of federal loans and block grants—as much as 25%—would be reserved for the zone.

Not everyone in the GOP is convinced that it is necessary to come up with a palatable alternative to affirmative action. Republican National Committee Chairman Haley Barbour insists that "we already have the high ground, and we don't need to do anything other than to be equal opportunity advocates against discrimination of any kind." With a packed legislative calendar, Congress won't have much time to deal with the inner city this fall.

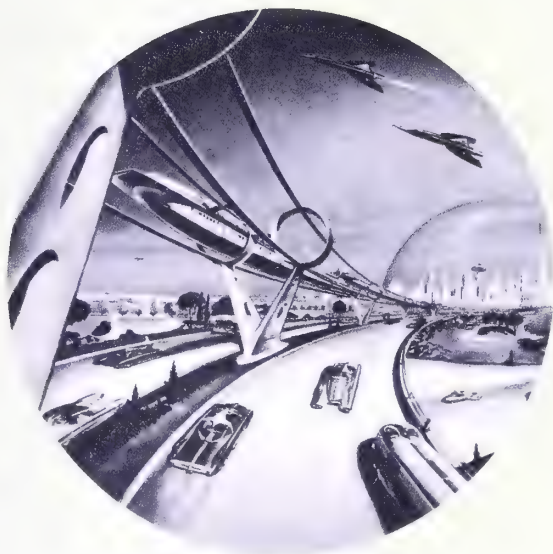
But GOP supporters are counting on the wider appeal of tax breaks to business and investors to help move the legislation early next year. Senator Abraham also intends to line up Republican governors and many Democratic mayors for a major lobbying blitz. While GOP Presidential hopefuls hammer away at affirmative action almost on a daily basis, minority voters are going to be demanding GOP alternatives. Kemp claims to have the ready-made answer.

*By Paul Magnusson in Washington*

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# WARP SPEED IN THE HIGH SEAS

Jet freighters could cut transatlantic voyages in half

The world's shipping lines are racing to put ever-larger superfreighters to sea. But naval architect David L. Giles thinks this competition with size is a fight among equals. No matter how big cargo gets, they will always lumber along at roughly 20 knots. For landlubbers, 23 mph.

What shippers really need in today's just-in-time markets, Giles insists, is greater speed. So he wants to see a sleek new breed of freighter that marries jet-ski technology to a hull design 100 feet shorter than a conventional superfreighter. These jet freighters could slice through mountainous waves at full speed and cut transatlantic voyages in half, to less than four days. They would charge up to twice the ordi-

nary rate for sea freight, thus making up for their higher fuel costs. Says Giles: "This ship is going to do for the movement of things exactly what the Boeing 707 did for the movement of people."

**ATLANTIC EXPRESS.** Giles has made believers out of engineers at the Massachusetts Institute of Technology who have performed computer simulations on his design and recommended improvements. MIT aeronautics professor Robert W. Simpson says Giles's startup, FastShip Atlantic Inc. in Alexandria, Va., could become the Federal Express of seagoing cargo: "It's going to be a very big business."

FastShip Atlantic has many a league to go before that happens. The biggest ship launched so far is a 23-foot-long model, whereas working vessels would stretch to 863 feet. And while the company has \$11 million in the bank, it needs \$800 million to build four ships and have some working capital.

Traditional shipping giants aren't investing in FastShip—SeaLand Inc., for one,

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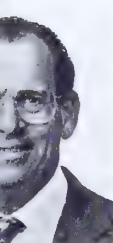
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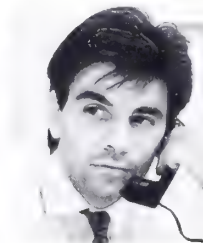
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## Industries

concluded that fast freighters were economical after building eight of the called SL-7s, in 1971 and 1972. It so them to the Navy.

FastShip Atlantic executives vow torpedo doubters by starting construction of the first ship by mid-1996. 1998, they assert, FastShips will whisking Bose stereos and Kodak film Europe, with Volvos making the t back. By shrinking their in-transit inventory costs, manufacturers could save money even after paying premium rates, says David B. Merchant, transportation director for Eastman Kodak Co. Volvo

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| <b>TECHNO-<br/>SUPERLINER</b> | 1,000             | 50               | NA                        |

\*TRANSATLANTIC  
NA - not applicable, since the TSL won't run on the Atlantic  
DATA: FASTSHIP ATLANTIC INC., SHIPPERS, BUSINESS WEEK

Transport Corp. bets it could cut \$3 million from its inventory in a single stroke by switching to FastShip.

These would-be customers aren't surprised by the shipping industry's c shoulder. In the global shipping cargo whose members meet to fix rates a service terms under antitrust immunity, "there isn't a lot of incentive for creativity," says Roger W. Wigen, 3M's transportation policy manager.

The technology works, at least in prototype. In trials in July in Göteborg, Sweden, the 23-foot model plowed through seas that loomed as large as 75-foot waves would to a full-size ship. "It exploded the wave—dissipated the crowds Giles. The FastShip has a deep V-shaped bow and grows flatter, even slightly concave, toward the stern. This prevents the stern from squatting down at higher speeds, and virtually eliminates the heaving in heavy weather that can crack normal hulls.

The latest design of the propulsion system calls for six General Electric turbines—modified models of the engine on 747 aircraft. Instead of propelling the turbines would drive five so-called

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## Industries

waterjets, which suck in water from lets beneath the hull and use spinning blades to pump it out the stern at high speed. The side jets would help steer while the big middle one, driven by turbines, is strictly for power. Waterjets already drive fast ferries plying the North Sea. FastShips would cruise 35 to 37 knots, or close to 43 mph.

Coupled with drive-through doors at the stern for speedy loading and unloading of cargo containers linked together in air-cushioned "trains," the results would be impressive: Door-to-door deliveries across the Atlantic would shrink to five to seven days. Conventional ships take 14 to 35 days, partly because they usually unload at seven ports. A FastShip would shuttle between two ports, carrying only 1,420-foot cargo containers, vs. as many as 6,000 in the latest container ships.

**PLAN B.** To realize the full benefits of the FastShip concept, ports would need special docks. That can get expensive. But Philadelphia officials, eager to boost their maritime business, have pledged \$7 million to help get FastShips underway—and \$75 million for a new terminal. The port's leading cargo handler, Thomas Holt Sr., has chipped in \$1 million for one-third ownership of FastShip Atlantic. The port of Zeebrugge, Belgium, is expected to spend about \$1 million to accommodate FastShips. German shipbuilder, Meyer Werft in Lingen, is negotiating to build them in the Philadelphia Naval Shipyard.

FastShip Atlantic will soon ask the U.S. Maritime Administration for \$10 million in loan guarantees as the anchor for private funding. If that fails, Plan B is to seek major financing from some shipper that's willing to break the mold.

FastShip isn't the only fast ship project around. In July, a Japanese consortium tested a small prototype of a waterjet-powered freighter designed to carry 150 20-foot containers at more than 45 knots. Dubbed the Tech Superliner, this miniship is aimed at short hauls around Japan and later the Asian mainland.

Giles is unbowed by the uncertainties. He believes he is heeding the advice of his famous father, the late yacht designer Jack Laurent Giles, who urged him never to waste time on projects that wouldn't succeed. His dad's maxim: "If you sink the boat, you drown yourself." Of course, Giles won't have to worry about his FastShips sinking unless he manages to get them afloat.

By Joseph Weber in Philadelphia with Ariane Sains in Stockholm and Edith Hill Updike in Tokyo



When birds of a feather  
flock together,  
they usually get plucked.

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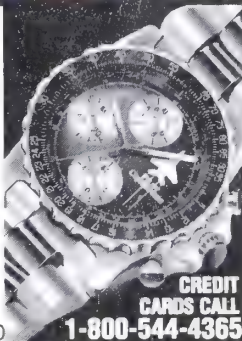
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## THE WASHINGTON ONLY LOCALS KNOW

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Time to burn. What to do?

Of course, you could always wait on an interminable line to see where the feds print the money at

the Bureau of Engraving & Printing, or watch from the Capitol visitors' gallery while some senator drones on about National Beef Week. But as any local will tell you, Washington is too vibrant a city to waste time maneuvering between gawking tourists and baby carriages at the National Air & Space Museum.

**EXOTIC FLORA.** Hidden amid the majestic monuments and halls of power, there are plenty of ways to enjoy a quick respite from Washington business while savoring a taste of the town. Knowing where to go is the key. Whether you're browsing through the bookstores and bistros along Connecticut Avenue north of Dupont Circle, or sampling delicate spring rolls and *Pho* along Vietnamese Row in Georgetown, Washington is filled with a dynamic inner life all its own.

Longtime denizens know the spots. Looking for solitude on a grand scale? Duck out to the U.S. Botanical Gardens, at the foot of the Capitol. The glass building houses an extraordinary collection of exotic flora. Or hop a cab to Dumbarton Oaks and meander across 10 acres of terraced gardens where

diplomats first hammered out the United Nations Charter. Then you can stroll through the oldest part of the city to Georgetown Park on M Street, an enclosed enclave of tony clothing and specialty shops. You'll probably recognize it as the backdrop of just

about every chase scene in Washington suspense thrillers, from *No Way Out* to *True Lies*.

Most visitors gravitate to the huge Smithsonian exhibitions clustered along the downtown Mall area. But these frenzied places, awash in T-shirt vendor trailers and hot dog stands, are shunned by us locals—except after snowstorms. There are richer jewels in some of the lesser-known museums around town. A personal favorite is the National Portrait Gallery and Museum of American Art, located on F Street between 7th and 8th Streets. With its ornate circular stair-

cases and atrium of stained glass, the building alone is a treasure. It features official portraits of every American President, plus a haunting exhibit of historical photos and paintings, many of them familiar masterpieces. It's not for kids—and it's only a block from Washington's Chinatown, where an excellent dim sum lunch can be had.

America's oldest museum of modern art, the Phillips Collection near Dupont Circle, is also more manageable than the hectic Smithsonian art-o-ramas. Another gem is the exhibit of famous scientific expeditions in anthropology, oceanography, and outer space in Explorers Hall on the first floor of the National Geographic Society, at 17th and M Streets. Or try the National Museum of Women in the Arts, at 13th Street and New York Avenue. While you're there, enjoy a cappuccino in the elegant café.

No local would deign to journey to the top of the Washington Monument except under extreme duress from out-of-town in-laws. There's a more splendid view

of the city—with no lines—atop the 315-foot clock tower of the Old Post Office



**HIGH LIFE:** *The Sky Terrace Restaurant is a Washington favorite*

Pavilion, on Pennsylvania Avenue between 11th and 12th streets.

But for a scene sure to faze you with Olympian hubris, throw back a few under the awning of the Sky Terrace Restaurant, atop the Hotel Washington across the street from the Treasury Building. Open through October, it's a capital favorite. Twilight is best, looking down on a vista that sweeps from the White House across the mall to the Potomac River to Arlington National Cemetery. Later, stroll the lobby of the el-

**TRANQUIL TERRACES:** *Dumbarton Oaks' gardens offer 10 acres of serenity*



**Where's the best view of the city? Atop the Old Post Office**





restored Willard Hotel next door. This is the place where 19th century do-wells, looking for and favors from Washington officials, once loitered. It was coined the term "ists."

**DANCERS.** Hungry? Accidental Grill, located in the same block at Pennsylvania Avenue and 15th Street, is a favorite restaurant for Washington power brokers. If you're feeling adventurous, try Marrakesh—a Moroccan restaurant at 617 York Ave. NW. Step through a narrow door into a room with a fountain and a carpeted dining room. The lounge on cushions, with their fingers off a tabletop while a belly dancer performs in dimmed light. A very exotic evening that's not as risqué as it sounds. But you'll need a taxi to get there and back, dinner starting at \$30 is

Georgetown features one

of the nation's premier supper clubs in Blues Alley at 1073 Wisconsin Avenue. A former carriage house, it's long been a showcase for jazz legends such as Sarah Vaughan, Ramsey Lewis, and Joe Williams. Creole dinners, too.

Still want to see some Washington politicians? La Colline, at 400 North Capitol Street, is a favorite lunchtime spot for U.S. sen-

ators. Try the lobster fricasee and look around—you'll likely see somebody you recognize. Ted Kennedy (D-Mass.) and Christopher Dodd (D-Conn.) are regulars. Afterward, take a walk across the street to painstakingly restored Union Station; the architectural grandeur is guaranteed to knock your socks off.

A favorite lunchtime hangout of Republicans is

## Getting There

**BY CAB** Any attraction mentioned is less than a \$5 cab ride from downtown.

**BY SUBWAY** The Metro is perfect for quick jaunts everywhere except Georgetown. For the Hotel Washington, take the Red or Blue lines to Metro Center; National Portrait Gallery, the Red or Green lines to Gallery Place; the Phillips Collection, Red line to DuPont Circle; La Colline, Red line to Union Station; Old Post Office, Blue or Orange lines to Federal Triangle; and Bombay Club, Blue or Orange lines to Farragut West. All trips, about \$1.

Galileo, a great Italian restaurant on 21st St. between L and M Streets. Try the mozzarella chunks with tomatoes and basil as an appetizer. Senate Majority Leader Bob Dole (R-Kan.) has a regular table against the far wall. For Clintonites, there's the Bombay Club at 815 Connecticut Avenue—a short walk from the White House. With its tropical white decor and Raj-style cuisine, this is a favorite lunchtime spot for everyone from Presidential advisers to Food & Drug Administration head David A. Kessler. Even the President has been known to sneak over occasionally for dinner.

But the locals know that the preferred time for a power meal in Washington is 8 in the morning. One power breakfast hot

spot is the elegant Hay Adams Hotel, located across the street from the White House. Or try the Sheraton Carlton at the corner of 16th and K Streets. You may not spot any powerful bigwigs, but you'll feel like one in settings that are vintage Washington.

Remember, if you have the time, Washington has plenty to offer. Just ask the locals. *Doug Harbrecht*





## AN OTTER'S-EYE VIEW OF MONTEREY BAY

Silicon Valley is a high-tech mecca, but outside its hermetically sealed, futuristic havens and sculpted office parks are the realities of a crowded industrial zone: clogged freeways, smog, and strip malls that don't exactly inspire business travelers to stick around when work is done. Of course, many visitors just zip an hour north to San Francisco. But for an offbeat, outdoor, and often spectacular day trip from the Valley, consider a 90-minute drive southwest to seaside Monterey.

Some people hear about Monterey and neighbor Carmel, and one word comes to mind: Fore! A round at Pebble Beach or one of the area's other fabled golf courses amid gnarly Monterey cypress is a wonderful day's outing. But if you're a bit more adventurous, con-



Grand Canyon. The sardines all but vanished in the 1940s, but the area's underwater geography is rich in other sea life. Otters, sea lions, and porpoises abound, and a forest of kelp species rises up from the ocean floor.

**ASK QUESTIONS.** Monterey Bay Kayaks (800 649-5357) sends about 7,000 visitors onto the bay annually to explore the kelp beds and soak up the scenery. You can rent kayaks by the hour and paddle around yourself or try one of their popular guided tours of Monterey Bay's southern shore. Monterey Bay Kayaks' marine-biology-savvy guides enjoy answering questions.

On a tour, participants pay \$45 for an hour of kayaking instruction and about three hours of paddling. Monterey Bay Kayaks routinely hosts work outings with groups from Silicon Graphics, Oracle Systems, Hewlett-Packard, and other Silicon Valley companies, but it's a great excursion for active business travelers who pack light: All the necessary wet suits, life jackets, and other gear are supplied.

First, paddlers head through a harbor area alive



**GUIDED KAYAKING:** A placid ride, all gear included

with seabirds, sailboats, and marinas. You're likely to spot a herd of California sea lions sunning on a rock jetty or popping up in the water to get an eyeful of you. But don't even think about touching them: Monterey Bay is a marine sanctuary, and all wildlife are protected.

You cruise along the wharf area, and soon, the water thickens with olive-green fronds of giant kelp, one of the bay's key ecological features. Colorful shellfish ride the flat kelp blades, and playful sea otters are a common sight here.

You don't have to be in great shape to enjoy a few hours of kayaking, a sport that's "quiet and nondisruptive," says Monterey Bay Kayaks owner Cass Schrock. "Almost anyone can do it"—except small children. The sea is usually fairly calm and requires only that you pay attention to navigate safely.

## Getting There

**BY CAR** Monterey is a 60-mile, 90-minute drive from San Jose. Take Route 101 South to Highway 156, then cut over west to Highway 1, the coast route. Follow Highway 1 south into downtown Monterey. Monterey Bay Kayaks is at 693 Del Monte Ave.

Continuing to paddle along the wharf, ahead you'll see the modern architecture of the world-renowned Monterey Bay Aquarium (408 648-8888). Don't miss a visit there, either before or after your otter's-eye view of the bay. Run by Hewlett-Packard founder David Packard and daughter Julie,

## DAY TRIPPING Silicon Valley

the aquarium is a showstopper. There's a three-story hall with a tank that illuminates "hold fasts" that anchor amazingly tall kelp plants to the sea floor. In the aquarium's outdoor pool, waiters prepare rescued otters to return to the ocean. And even adults love hands-on "touch pool" where you can handle the textured "Turkish towel" weed, or pet a bat ray.

Both paddling the bay and learning about its bounty at the aquarium are enough to make any visitor want to delve more deeply into marine biology. Thanks to Monterey Bay Kayaks' Web page <http://montereykayaks.com>, you can do just that before or after your visit. There's even a link to a video camera trained on Monterey Bay providing up-to-the-minute weather conditions. But don't let that keep you home; a virtual Monterey Bay is a pale substitute for the thing. *Joan Hamlin*



**SWIRL OF ANCHOVIES:** An aquarium like no other

sider experiencing the area from a different vantage point: sea level. A few hundred yards off Monterey's wharf, once home to two dozen booming sardine canneries and the backdrop for John Steinbeck's *Cannery Row*, begins an oceanic canyon extending 100 miles west and deeper than the



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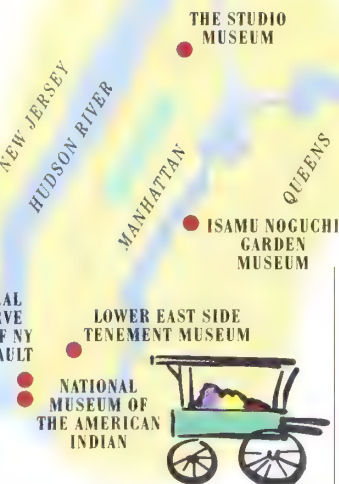
## A HELLUVA TOWN FOR OFFBEAT MUSEUMS

Next time you're hungry to go museum-hopping in New York, don't instinctively bolt

for warhorses such as the Metropolitan or the Guggenheim for the umpteenth time. Instead, choose one of the city's smaller, off-beat museums. You can visit them in as little as 45 minutes—an ideal respite for a traveler with a meeting-packed day. And the memories could last a lifetime.

To escape the relentless speed and growling traffic of Manhattan streets, the contemplative Isamu Noguchi Garden Museum in Queens—complete with chirping birds and weeping cherry trees—is the perfect retreat. This indoor-outdoor gallery, opening into a sculpture garden, was the workshop of Japanese-American sculptor Isamu Noguchi (1904-1988). His abstract compositions, carved out of marble and granite boulders, avoid being for connoisseurs only, and some works are truly spellbinding. My favorite: an outdoor sculpture fountain that has a hypnotic effect as water spills gently over the rim of a salt basin.

**IMMIGRANT LIFE.** If cross-cultural modern sculpture sounds too cerebral, try the more down-to-earth Lower East Side Tenement Museum, at 90 Orchard St. Here you will be taken on a tour through one of the dark and dingy buildings that housed immigrant Jewish and Italian families at the turn of the century. You'll



**DAY TRIPPING**  
New York City

get a good sense of the cramped living conditions of the time as well as a whiff of the malodorous, windowless rooms. The trophy is an original, soiled water closet with

newsprint pinned to the wall for toilet paper. (New Yorkers apparently took to recycling early.) The surrounding neighborhood is still the first stop for the city's current wave of Chinese immigrants—whose living condi-

tions are not much better.

If you prefer riches to rags, a visit to the gold vault of the Federal Reserve Bank of New York at 33 Liberty St. could be fun. It must be booked at least a week in advance (212 720-6130) but it's worth the extra planning. Locked behind steel bars, buried five stories below street level, the world's most-guarded "inmates"—about 10,000 tons of gold ingots—are stashed away in a basement half the size of a football field. The vault

houses \$126 billion worth of gold belonging to foreign central banks, causing the New York Fed to sit atop the world's largest gold cache. Luckily, the stuff still hasn't sunk as low as Vladimir Lenin prophesied: "When we are victorious on a world scale," he wrote, "we shall use gold for the purpose of building lavatories in the streets..."

**INTERACTIVE TRIBE.** If you have any interest in ethnic art, don't miss the revamped National Museum of the American Indian, located in the palatial U.S. Customs House building at One Bowling Green in Lower Manhattan. I was taken aback by the museum's innovative way of displaying art: You can use interactive videos to put the work into context or join a "talking circle," a workshop in which Native Americans who still live

## Getting There

**BY CAB** Each museum mentioned is less than a \$5 cab ride from downtown hotels or offices, except for the Isamu Noguchi Garden Museum at 32-37 Vernon Blvd. in Long Island City, Queens (about \$14), and the Studio Museum at 144 W 125th St. (between Lenox and Seventh Avenue) in Harlem (about \$20).

on reservations talk about their lives, tribes, beadwork and art with visitors.

Ironically, the Custom House that holds the art was built at a time when many believed Indian culture would disappear in the wake of Western civilization. One of the sculptures is a female figure, representing America, crushing an Aztec deity underfoot.

Another gem beyond the usual Manhattan haunts is the Studio Museum in

Harlem, one of the nation's premier venues of African American art. From one of the gallery's windows, you can glimpse a burned-out tenement house, parts of which have been used in one of the works currently on display.

In fact, much of the art reflects the rough edges of urban surroundings, such as poverty and drug use. Don't let that deter you from exploring the neighborhood. The museum is in the block between 125th and 130th Street shopping district where you'll find everything from African fabrics to genuine hair wigs and extensions. After all, New York's museums are its living, breathing neighborhoods. permanent display and free charge.



**THE STUDIO MUSEUM:** A portrait by Fred Brown



**NOGUCHI GARDEN MUSEUM:** Songbirds and sculpture



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## TOURING THE TOWERS —BY BOAT

Chicago is a town of vibrant ethnic neighborhoods, outstanding museums, and hip and sophisticated nightlife. But if you've got only a couple of hours between meetings to sample its glories, take a boat ride on the Chicago River. Not just any tour, but the cruise run by the Chicago Architecture Foundation. On board Chicago's First Lady, one of the world's most gorgeous skylines comes to life as you snake through downtown and into Lake Michigan.

The river is a showcase for some of the 20th century's most striking buildings and most influential architects—the art deco firm of Holabird & Root, the steel-and-glass-box modernist Ludwig Mies van der Rohe, and many of his followers at vast Skidmore, Owings & Merrill. Such is Chicago's standing in the world of architecture that "outsiders" such as Philip Johnson and Kevin Roche came to town in the late 20th century to put up important new buildings. Up and down the river, the new pays hom-

### Getting There

**BY CAB** Chicago's First Lady departs from the south side of the Chicago River at Michigan Avenue and Lower Wacker Drive downtown. It's less than a \$5 cab ride from any downtown hotel. Take the curved stairs down to the boarding area. The 90-minute cruises are scheduled at 9:30 a.m., noon, and 2 p.m. through Sept. 30. Then, at noon Monday to Friday, and at noon and 2 p.m. on weekends through Oct. 29.

age to the old: Just look at the flying buttresses on the neo-deco NBC Tower, built in 1989, similar to those on the nearby soaring neo-Gothic Tribune Tower, vintage 1925. **DECO DELIGHTS.** The tour, led by an expert from the architecture foundation, begins beneath the Beaux Arts-style

The boat heads east, past former wasteland now transformed into bustling offices and apartments, onto Lake Michigan. As the craft swings 'round toward the city, in the distance can be seen mile-long Navy Pier, built in 1916 but recently reopened as a collection of shops, soundstages, and a brand-new Ferris wheel. More stunning is the skyline to the west and south. Along Michigan Avenue, a phalanx of handsome

trict, you pass an explosion of styles and colors. Unmistakable is the hulking, 4-million-square-foot Merchandise Mart, an art deco limestone behemoth with gothic leaf running across the top. Original owned by Marshall Field family, passed to the Kennedy family in the '40s. Directly across the river, there's the neo-classical R.R. Donnelley Center, built in 1992, with its soaring windows set off by narrow



**GRANDEUR:** Ogling the Wrigley and IBM buildings from the river

Michigan Avenue bridge. Around you are some hallmarks of the 1920s Golden Age. Just north sits the white, terra-cotta Wrigley Building, with its clock tower, designed by Graham, Anderson, Probst & White in 1924. Across the street is the Tribune, a product of an international design contest. On the south bank are two significant art deco designs—Holabird & Root's 333 N. Michigan and Alfred Alschuler's 360 N. Michigan, replete with columns and a colonnade at the top. A more modern influence waits just downriver: Mies's last major commission, the black-iron-and-glass IBM Tower (1971).

structures built after the devastating 1871 Chicago Fire comes into view. In the foreground is the gray-white, spare but sturdy Amoco Building—Chicago's second-tallest—designed by Edward Durrell Stone in 1974.

As the boat winds back into the river and the heart of the business dis-

trict, you pass an explosion of styles and colors. Unmistakable is the hulking, 4-million-square-foot Merchandise Mart, an art deco limestone behemoth with gothic leaf running across the top. Original owned by Marshall Field family, passed to the Kennedy family in the '40s. Directly across the river, there's the neo-classical R.R. Donnelley Center, built in 1992, with its soaring windows set off by narrow

row strips of concrete. Its neighbor to the south is arguably Chicago's most striking late-20th-century building: the green-glass, 333 W. Wacker Building, which snakes for 365 feet along the curve of the river. Designed in 1983 by Kohn, Pedersen, Fox, with Perkins & Will, it picks up reflections of the clouds and the Mart across the way.

The final stretch of the tour reaches downtown into the Loop—past a collection of Skidmore, Owings & Merrill boxes that derive much from Mies. Soaring above it all, of course, is Skidmore's 1974 showpiece the Sears Tower, the world's tallest building. As the boat heads for home, you spot the highly idiosyncratic building of a type oddly comfortable in Chicago. There's Kohn, Pedersen's postmodern octagonal office tower, a hodgepodge of styles topped with what appears to be

strange, white minaret-like, which glows like a lantern-like at night. Nearby is Bertram Goldberg's River City apartment-and-marriage complex, whose square concrete structure with bubble-shaped windows remind you of a modernist's All of an open porphyry granite. In Chicago architecture, it seems, even the most eclectic has its place. *Rick Melnick*







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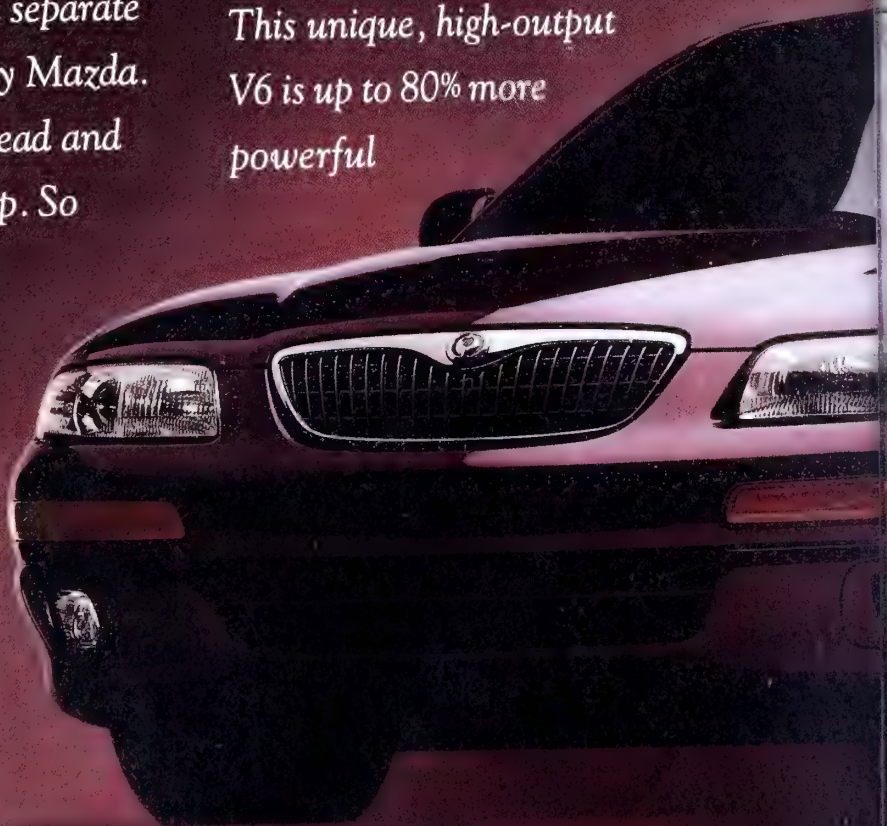
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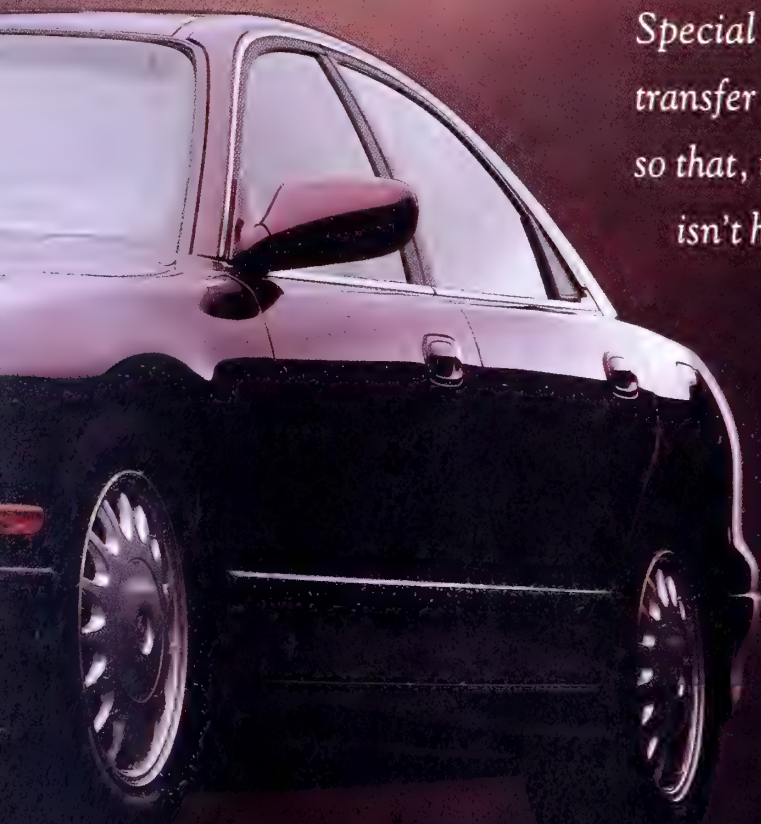
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PITTSBURGH



FALLINGWATER

## Pittsburgh department-store magnate Edgar J. Kaufmann had a chunk of

Pennsylvania highlands with a waterfall. He hired an architect and said he was willing to spend \$30,000—a nice piece of change in 1934—for a house with a view of the falls. In the end, he spent five times that much

and didn't even get the view. Instead, architect Frank Lloyd Wright built the house, Fallingwater, right on top of the falls. "I want you to live *with* this waterfall, not just look at it," explained the legendary architect, who treated even his most powerful patrons like pupils.

**HIGHLAND DRIVE.** Indeed, Fallingwater, with its cantilevered decks and rough sandstone walls, seems an outgrowth of the stream, Bear Run. The cascading water can be heard throughout the house, now a museum operated by the Western Pennsylvania Conservancy for the last 32 years, even over the voices of tour guides and the footsteps of legions of awed tourists. So, despite the human hubbub, Fallingwater remains a refreshing getaway two hours east of Pittsburgh.

After making a reservation by telephone (412 329-8501), I took a pleasant drive through Pennsylvania's gently rolling Laurel Highlands. I went on a weekday, ex-

## FRANK LLOYD WRIGHT'S WATERWORLD

pecting a guide to leisurely lead three or four of us through the house. No such luck: Cars were lined up at the gate, and would-be parkers were already being diverted to the overflow lot. The crowded entrance pavilion, café, and gift shop seemed more like Seaworld than a rustic getaway. And the din of a chain saw-wielding work crew, lustily intent on building some sort of wooden pagoda before lunchtime, was jarring.

But the racket faded as the 15 of us in the 11:47 a.m. group trekked down the

forest path, through the mountain laurels and rhododendrons, toward Fallingwater. Along the way we saw plenty of the horizontal formations of buff-colored sandstone that are repeated in the walls of the house.

I believe that if Wright had lived into the 1990s, he might have altered the outside of the building. To the jaded modern observer, the concrete decks recall... well... downtown parking garages. Of course, this might not have been the result if Kaufmann had followed the architect's instructions to the letter and covered the concrete with gold leaf. Instead, the retailing tycoon decided to save himself a few

bucks and painted the concrete ocher.

But what made Fallingwater particularly moving for me was the interior. Expecting to appreciate the home simply as a work of art rather than as a comfortable abode, I stepped inside only to discover that it's nothing less than a dream house. The ceilings are low, like the rock

front of the fireplace. Wright wanted to cut it down floor level but deferred Kaufmann, who suggested leaving it intact. And Wright designed a d. Kaufmann considered small, the customer explained: "This isn't enough for writing checks, architects." Wright enlarged it.

**HISTORICAL HIKES.** If you have business in Pittsburgh, Fallingwater is an ideal trip on its own. But if you have extra time, Ohio State Park, with its wild water rapids and abund-



**STREAMLINED:** The falls can be heard throughout the house.

ledges outside, and the dark and narrow hallways are almost like caves. But each room, with its marriage of indoors and outdoors, begs to be enjoyed, to be lived in. If only they'd let you sit on the furniture, kick up your feet as the Kaufmanns did, take in the view of Bear Run, and maybe drink a cup of steaming coffee over by that Picasso...

Sorry. The 45-minute walking tour keeps you walking. And handling the furniture—let alone sitting on it—is strictly verboten. Luckily, the tour is filled with fascinating tales of testy relations between the strong-willed architect and his equally headstrong patron. Surprisingly, Kaufmann actually won a few of the jousts. In the living room, for example, a boulder rises through the floor in

hiking trails, is five miles the south. And 10 miles is Fort Necessity, the Revolutionary British post where a young George Washington got his taste of battle in the French Indian war. (Unfortunately he lost.) Park hosts described in vivid detail the life of an 18th-century soldier, lived on hardtack and on dirt, rarely getting to change his clothing. It's certainly a miserable sentence, especially when compared to the Kaufmann meticulously planned paradise nearby.

Fallingwater is open a.m. to 4 p.m., every day except Monday, until November and then only on weekends through March. Admission is \$8. But remember to call in advance—it's sure to be busy. *Stephen E.*

## Getting There

**BY CAR** From downtown Pittsburgh, take Route 376 east 10 miles to the Pennsylvania Turnpike, Route 76. Take the Turnpike east to Exit 9 (Donnegal). Go left on Route 31 for two miles, then turn right onto Route 381 South for 19 miles.

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# WORK

# PLACE

H O T E L



## THE OTHER NIAGARA: A JEWEL ON THE LAKE



### Niagara-on-the-Lake offers business travelers the perfect escape from

fast-paced Toronto. Outside of rush hour, it's an easy 90-minute drive from Canada's business capital. But once you arrive, you'll feel as if you've traveled back a century.

This charming town of 13,000 nestled along the shores of Lake Ontario at the mouth of the Niagara River—and a world apart from the carnival atmosphere of well-known Niagara Falls, Ont.—is one of North America's best-preserved 19th-century villages. That's appropriate, since the town and surrounding Niagara Peninsula saw some of the fiercest fighting during the War of 1812. Today, Niagara-on-the-Lake is also home of the renowned Shaw Festival, a repertory theater that from spring to early autumn performs works by George Bernard Shaw and his contemporaries. And it's at the center of Ontario's rapidly improving wine industry.

Early fall—September and October—is arguably the best time to visit. The town is less crowded than during peak summer season. And the Niagara Parkway, running 13.5 miles along the Niagara River gorge down to the world-

famous falls, is spectacular once the leaves start to change by late September. That's also when the grape harvest kicks off at the area's vineyards. And this fall, the Shaw Festival will be in full swing until Oct. 29.

Delve into the area's history starting at Fort George, a huge British-built fort at the edge of town, which has been restored to the way it looked on the eve of the War of 1812. From there, the short drive to Niagara Falls passes several other monuments, including a Georgian-style farmhouse that served as a military hospital, and the homestead of Laura Secord, the beloved Canadian heroine who alerted her country's forces to an American invasion. Best of all, the scenery is some of the nicest in Ontario.

**VINE DRIVE.** The "Wine Route" established by Ontario's vintners also passes through Niagara-on-the-Lake. This well-marked drive includes more than 25 wineries, many run by first-generation German immigrants attracted by the region's fine growing conditions. Although many of these wineries are upstarts by European stan-

**DAY TRIPPING**  
Toronto

### Getting There

**BY CAR** From Toronto, take the Queen Elizabeth Way (QEW) south toward Niagara Falls. After passing St. Catharines, take Exit 38B onto Highway 55, which runs into Niagara-on-the-Lake. The drive takes 90 minutes.

**HISTORY TOUR:** The area saw some of the fiercest fighting of the War of 1812



**VINTAGE VIEWS:** Inniskillin winery offers self-guided t

dards, they've garnered an impressive number of international awards in recent years. Most offer tastings for a nominal charge. The best introductory tours are offered by Inniskillin and Hillebrand Estates, both near the town. Inniskillin offers a fascinating self-guided tour which explains how it and other local wineries make some of the world's finest "icewines." This sweet desert wine is made from grapes harvested only after they've frozen on the vine.

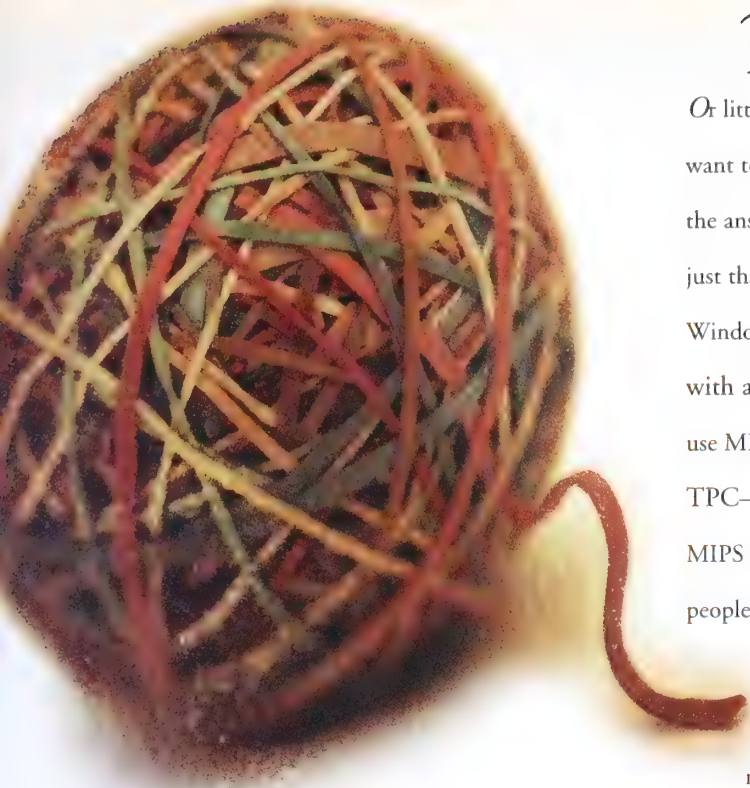
While many Torontonians consider Niagara-on-the-Lake a day trip, you'll find it more relaxing if you stay overnight. Because rooms are at a premium, call the accommodation service offered by the

Chamber of Commerce (468-4263) before you go. It can help you find a room, the town's best hotels. Of them, the Prince of Wales and Queen's Landing, have excellent restaurants. For a more memorable stay, ask the Chamber to help book a night in one of the town's 86 bed-and-breakfasts. Many are beautifully served homes in the historic district. And all have inspected for compliance with the town's quite high standards. Rates mostly range from \$50 to \$100 a night, including breakfast. With Canadian dollar worth just U.S., bargains abound.

A perfect way to spend your evening is at the Shaw Festival, which is staging nine plays into the fall, including a brilliant revival of Noel Coward's epic *Cavalcade*. Be sure to call ahead for tickets (800 267-4141). They normally cost under \$45 U.S., but Sunday evening performances are \$19.

Many Canadians secretly happy to see more Americans have heard of Niagara-on-the-Lake. Too many visitors, they argue, would spoil the place. If you're lucky enough to go, you'll no doubt agree. *Bill Syme*





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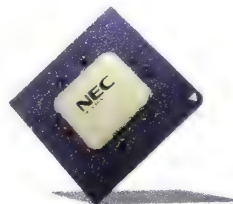
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## A WALK THROUGH FEUDAL JAPAN



Tokyo has rebuilt itself so often that few visible traces remain of old Edo, as the

feudal city was known until this century. Thanks to seemingly constant construction after earthquakes, fires, and war, Tokyo has emerged as a city that is at times antiseptically modern—in stark contrast with most Westerners' romanticized fantasy of ancient Japan. But Kawagoe, the prosperous castle town just an hour away that is nicknamed "Little Edo," preserves a taste of merchant Japan in the days of the shoguns—and not just in temples and shrines.

Kawagoe's main shopping street houses several century-old buildings called *kura*, combination shop/homes with

### Getting There

**BY TRAIN** Take the Seibu Shinjuku line from beneath the Seibu Prince Hotel or Takadanobaba Station. It's a 45-minute ride to Hon-Kawagoe station, and tickets cost ¥550. Explore on foot from there.

blackened clay-and-plaster walls two feet thick, most still in use.

The shopping street runs north from Hon-Kawagoe station (the preferred of the town's two rail stations, since it is within easy walking distance of the historic area). Although narrow by today's standards, this street was once considered a broad thoroughfare and was a well-used commercial route where much of the traffic was man-powered.

The first *kura* you come to, after the third traffic light, is the Yamazaki Museum (admission: ¥500, including tea). The small museum displays a mishmash of screen paintings, Noritake china, candy-making molds, coins, and

elaborate candy sculpture made at

Kameya, a 200-year-old sweet shop next door. Giant stone blocks pave the inner courtyard. The beams are thick and dark, the ceilings low, and the windows heavy to lock out fire. (Labeled by Japanese proverb as one of the four greatest fears in this land of traditional wood and paper houses, fire destroyed most of central Kawagoe in 1893. The *kura*, however, survived.)

**TREASURE.** *Kura* have other special connotations for the Japanese. Most were used for storage, especially of valuables, and even today, treasures occasionally are discovered in the dark corners of such storehouses near much-older Kyoto. But *kura* also were places to shut up a mentally ill relative or a

young mistress—a place of dark and narrow staircases, small windows, shadows, and ghosts.

Continue walking up the street and you will see several other *kura*, mostly on the left-hand side. At one corner is pottery shop Yamawa, with an old man-powered *jinrikisha* displayed by the side entrance and a wide selection of intriguing ceramic designs. Two doors down is silk-scrum maker and art dealer Ichiro Fukazen, the fifth generation

twisting staircase on ear. The Y100 admission includes an English brochure and good map of other near sights.

**FIRST SHOGUN.** One of the largest is the Kita-in temple complex, with entire buildings transported from Edo Castle in Tokyo, a sculpted garden of 500 Buddhas and quiet, pleasant grounds. There is some interesting history, too. Kita-in was the head temple of the Buddhist Tendai sect in eastern Japan.

**KAWAGOE:** Many century-old buildings have survived



and the first shogun Tokugawa Ieyasu, a close friend of the head priest. As a result, the land at Kita-in was owned and run by *bakufu*, the Shogun's no jurisdiction the Rear access to grounds is through what is known as Thief's Bridge, once a simple log across a river over which a thief escaped. He was later forgiven for crime after being converted to the path of virtue by the head priest.

For travelers with more time—and money—a trip to ancient Kyoto via Japan's bullet trains would provide much deeper insight into Japan's rich history and culture. But if you or other pressures take you to Tokyo, Kawagoe can be surveyed in an afternoon, and you come away with an experience missed by most

visitors to the ancient capital. Be forewarned: You'll find difficulty finding English spoken in Kawagoe, even the town's visitor center. Anyone can point you toward the *kura*. Besides, a close look at the real Japan, what this day trip is about.

Edith Up

## One silk-scroll maker here is the fifth generation to ply the trade

of his family to ply the trade. If you've a mind to shop, prices are moderately better here than they are in Tokyo. At the end of the row, the Kurazukuri Museum, formerly a tobacco merchant's shop, gives the best look inside a *kura*, with what seemed to me to be the narrowest



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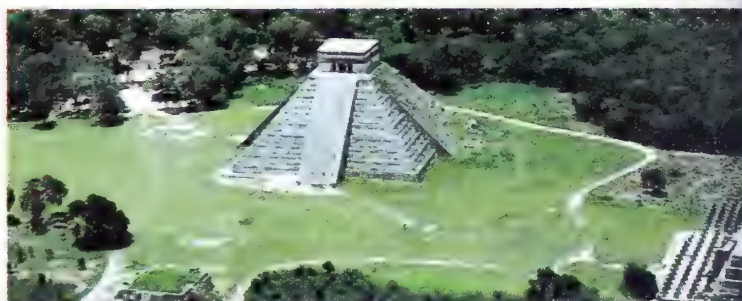
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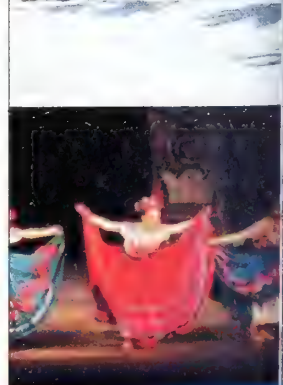
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# HERE VAN GOGH'S T FOR LIFE ENDED



of tourists who crowd the rooms and click cameras at the water lilies—even during the less frantic autumn season—can be overbearing. In contrast, Van Gogh's town of Auvers-sur-Oise is relatively empty, and it offers a more intense experience. The stone village and open countryside, remarkably unchanged since Van Gogh painted them, draw you into the lonely, brooding vision of this great post-Impressionist artist.

The trip has become even more appealing since the recent restoration of the café below Van Gogh's garret. Bought by a Belgian businessman, the Auberge Ra-

## DAY TRIPPING Paris

voux now looks just as it did in 1890, from the cracks in the plaster of Van Gogh's room to the billiard table where his casket was laid for a funeral service. You can buy art books and prints and see a short video of his life—viewed by an audience of four on one recent summer weekday. Showings are daily except Monday from 10 a.m. to 6 p.m.; entry, \$5 (331 3448-0547).

Visit the café first to learn about the artist. Then, avoid-



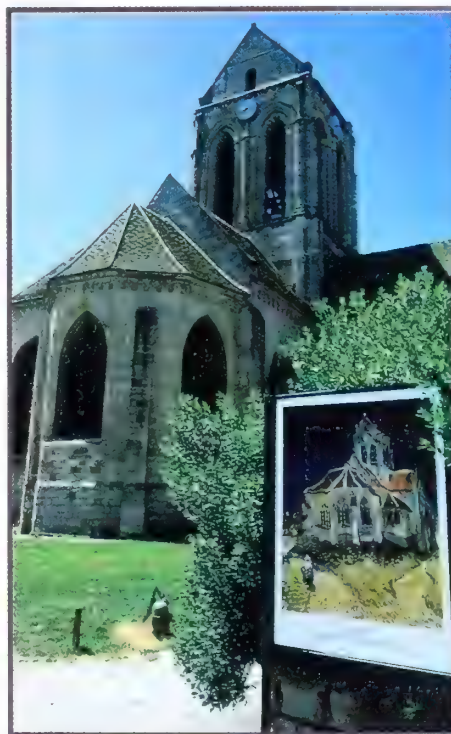
cracks in the plaster of Van Gogh's room to the billiard table where his casket was laid for a funeral service. You can buy art books and prints and see a short video of his life—viewed by an audience of four on one recent summer weekday. Showings are daily except Monday from 10 a.m. to 6 p.m.; entry, \$5 (331 3448-0547).

fter painting 70  
es in 70 days,  
gh shot himself

ing the drab highway through town, stroll along the parallel hillside street of old stone houses. Finally, climb to the cemetery where Van Gogh lies inconspicuously next to his brother, Theo, against the north wall.

On this walk, you'll see several roadside posts holding photos of Van Gogh canvases that were painted at those spots. The most en-

**ART AND MODEL:** *Many sites, like this church, display Van Gogh's vision of them*



trancing site lies down a dirt road opposite the cemetery gate. There, Van Gogh painted *Crows over the Wheat Field*, a dark, haunting picture that some experts think was his last. The scene

hasn't changed. The artist borrowed a gun to shoot crows here, claiming they disturbed his work. He used it on himself instead.

**PICNIC PLACE.** Auvers lies on the Oise, a broad, placid river with grassy banks that cry out for a picnic once you're through wandering. The town has a few so-so cafés, or you can have a full-course French meal in the courtyard at Van Gogh's Auberge Ravoux, which is open at lunch and for dinner from 8 p.m. to 10 p.m. (\$28 plus beverage).

Trains run almost hourly to Auvers from the Gare du Nord and Gare Saint-Lazare in Paris. You must change trains en route. Beware: Check before you board because connecting points vary depending on train and time of day. It will cost 56 francs, or about \$11 round trip, and takes no more than an hour each way. Auvers is also an easy hour's drive from Paris, but car rentals in France are expensive—especially for models

with automatic transmission.

Van Gogh's last home may not be on the major tourist circuits. But for that reason, you're likely to gain a deep, lingering new feeling for a great artist. *Stewart Toy*

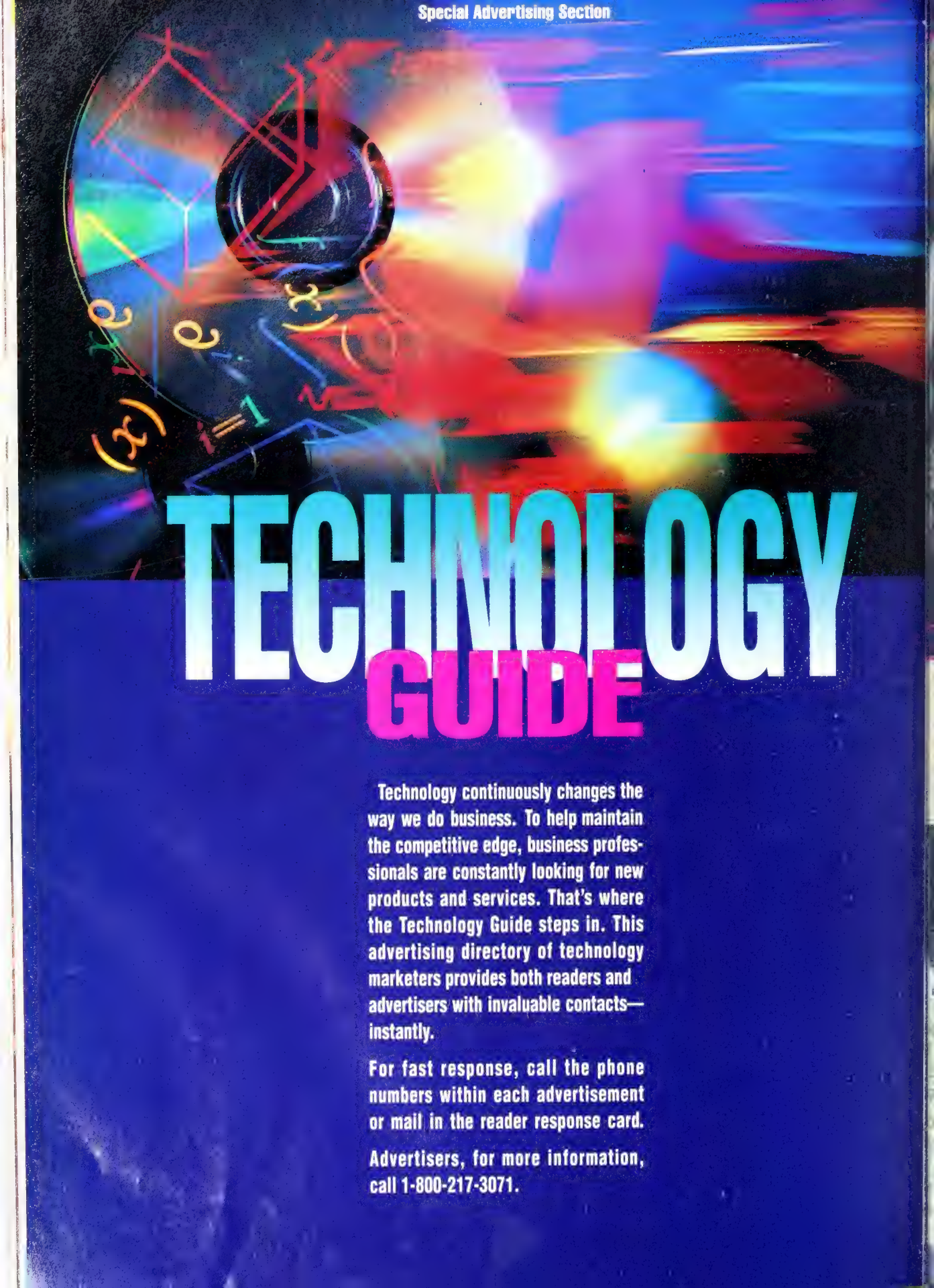
## Getting There

**BY TRAIN** Trains run almost hourly to Auvers from the Gare du Nord and the Gare Saint-Lazare in Paris. But note: You must change trains en route; ask at which station. The trip will take about an hour. Tickets, which cost about \$11 round trip, must be punched in an orange ma-

chine near the platform before boarding.

**BY CAR** Take Autoroute A1 north from Paris, then Autoroute A86 west and later Autoroute A15 northwest toward Pontoise. Pick up Route D4 northeast into Auvers. The 25-mile drive takes under an hour.





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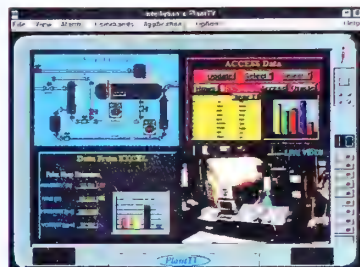


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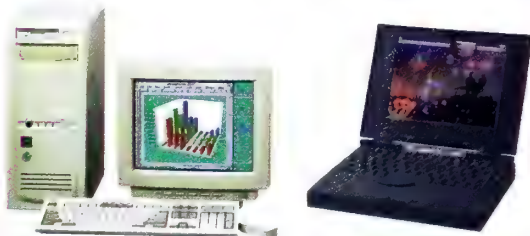
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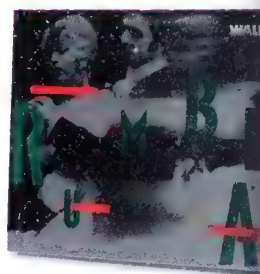
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# Business Week Index

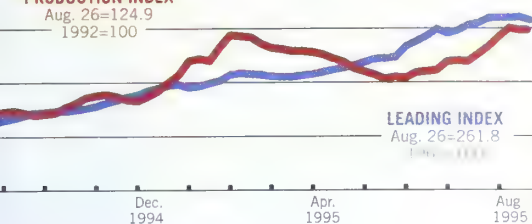
## PRODUCTION AND LEADING INDEXES

Change from last week: 0.0%  
Change from last year: 5.6%

Change from last week: 7.9%  
Change from last year: 7.9%

### PRODUCTION INDEX

Aug. 26=124.9  
1992=100



### LEADING INDEX

Aug. 26=261.8  
1992=100

These are 4-week moving averages

The production index was unchanged during the week ended Aug. 26. Before the index of the four-week moving average, the index rose to 126, from 124.9, because of increased seasonally-adjusted output of cars and trucks led the rise. The power fell back after large weather-related gains in previous weeks. The leading index fell in the latest week, but the unaveraged index increased 3, from 261.7. Faster growth in M2 and materials prices caused the

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## PRICING INDICATORS

|                                           | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|-------------------------------------------|-------------|-----------|--------------|
| <b>PRICES</b> (9/2) S&P 500               | 561.14      | 558.47    | 18.4         |
| <b>RATE BOND YIELD, Aaa</b> (9/2)         | 7.39%       | 7.60%     | -8.7         |
| <b>RAW MATERIALS PRICES</b> (9/2)         | 114.3       | 114.9     | NA*          |
| <b>INSURANCE FAILURES</b> (8/25)          | NA          | 283       | NA           |
| <b>STATE LOANS</b> (8/23) billions        | \$494.6     | \$493.5   | 12.3         |
| <b>SUPPLY, M2</b> (8/21) billions         | \$3,708.2   | \$3,699.3 | 3.6          |
| <b>CLAIMS, UNEMPLOYMENT</b> (8/19) thous. | 349         | 338       | 8.0          |

\*Center for International Business Cycle Research (CIBCR), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on failures and real estate loans. \*Historical data available from CIBCR

## INTEREST RATES

|                                                 | LATEST WEEK | WEEK AGO | YEAR AGO |
|-------------------------------------------------|-------------|----------|----------|
| <b>MUTUAL FUNDS</b> (9/5)                       | 5.86%       | 5.48%    | 4.74%    |
| <b>COMMERCIAL PAPER</b> (9/5) 3-month           | 5.77        | 5.80     | 4.92     |
| <b>SAVING DEPOSITS OF DEPOSIT</b> (9/6) 3-month | 5.75        | 5.76     | 4.89     |
| <b>MORTGAGE</b> (9/1) 30-year                   | 7.95        | 8.10     | 8.63     |
| <b>FIXED RATE MORTGAGE</b> (9/1) one-year       | 5.86        | 5.92     | 5.58     |
| <b>LIBOR (9/6)</b>                              | 8.75        | 8.75     | 7.75     |

Source: Federal Reserve, HSH Associates, Reuters Holdings PLC

Seasonally adjusted in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### PRODUCER PRICE INDEX

Friday, Sept. 12, 8:30 a.m. ▶ Producer prices of finished goods probably rose by 0.2% in August, says the median forecast of economists surveyed by MMS International of the McGraw-Hill Cos. If so, that would be the first increase in prices since 1994. Producer prices were unchanged in July. The volatile food and energy prices likely rose 0.2% in August, says the MMS survey. Both

### CONSUMER PRICE INDEX

Friday, Sept. 13, 8:30 a.m. ▶ Consumer prices for all items and prices, including food and energy, likely increased 0.2% in August, says the MMS survey. Both

the total price index and the core rate rose by 0.2% in July. Weak apparel prices and cuts in car prices because of dealer incentives probably offset gains in prices of other goods and services. Consumer inflation remains on track to rise about 3% in 1995, the same mild pace as in 1994.

### RETAIL SALES

Thursday, Sept. 14, 8:30 a.m. ▶ Retail sales probably rose a modest 0.3% in August, after falling 0.1% in July. Motor vehicle purchases were strong, thanks to rebates and other incentives, but many major retail chains reported weak sales. That's partly because the warm weather deterred people from buying cool-weather,

back-to-school clothing. Excluding cars, retail sales probably rose by 0.2% in August, on top of a 0.2% gain in July.

### INDUSTRIAL PRODUCTION

Friday, Sept. 15, 9:15 a.m. ▶ Output at the nation's factories, mines, and utilities probably rose 0.4% in August, forecasts the MMS report. That's suggested by the small gain in factory jobs and the increase in the workweek, including overtime. In July, industrial production rose 0.1% as the heat wave pushed up utility use by 3.6%. Factory output fell 0.2% in July, led by a steep decline in auto production. Operating rates for all industry likely inched up to 83.6% last month, from 83.4% in July.

## PRODUCTION INDICATORS

|                                                       | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|-------------------------------------------------------|-------------|-----------|--------------|
| <b>STEEL</b> (9/2) thous. of net tons                 | 1,949       | 1,904#    | 3.2          |
| <b>AUTOS</b> (9/2) units                              | 115,982     | 119,684r# | -9.2         |
| <b>TRUCKS</b> (9/2) units                             | 113,277     | 118,137r# | -2.0         |
| <b>ELECTRIC POWER</b> (9/2) millions of kilowatt-hrs. | NA          | 73,896#   | NA           |
| <b>CRUDE-OIL REFINING</b> (9/2) thous. of bbl./day    | NA          | 14,183#   | NA           |
| <b>COAL</b> (8/26) thous. of net tons                 | 20,317#     | 19,873    | -3.3         |
| <b>PAPERBOARD</b> (8/26) thous. of tons               | 890.4#      | 879.7r    | -0.8         |
| <b>PAPER</b> (8/26) thous. of tons                    | 851.0#      | 833.0r    | 0.2          |
| <b>LUMBER</b> (8/26) millions of ft.                  | 465.9#      | 452.1     | -2.4         |
| <b>RAIL FREIGHT</b> (8/26) billions of ton-miles      | 25.0#       | 24.4      | 2.5          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAA<sup>1</sup>, SFPA<sup>2</sup>, Association of American Railroads

## PRICES

|                                                           | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|-----------------------------------------------------------|-------------|----------|--------------|
| <b>GOLD</b> (9/6) \$/troy oz.                             | 380.050     | 381.650  | -1.7         |
| <b>STEEL SCRAP</b> (9/5) #1 heavy, \$/ton                 | 146.50      | 146.50   | 8.9          |
| <b>COPPER</b> (9/1) ¢/lb.                                 | 137.3       | 142.5    | 15.3         |
| <b>ALUMINUM</b> (9/1) ¢/lb.                               | 85.5        | 88.0     | 15.5         |
| <b>COTTON</b> (9/1) strict low middling 1-1/16 in., ¢/lb. | 90.55       | 89.77    | 27.0         |
| <b>OIL</b> (9/5) \$/bbl.                                  | 18.51       | 17.92    | 4.0          |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                                        | LATEST WEEK | WEEK AGO | YEAR AGO |
|----------------------------------------|-------------|----------|----------|
| <b>JAPANESE YEN</b> (9/6)              | 98.74       | 98.80    | 99.45    |
| <b>GERMAN MARK</b> (9/6)               | 1.48        | 1.48     | 1.56     |
| <b>BRITISH POUND</b> (9/6)             | 1.55        | 1.54     | 1.54     |
| <b>FRENCH FRANC</b> (9/6)              | 5.09        | 5.07     | 5.34     |
| <b>ITALIAN LIRA</b> (9/6)              | 1621.5      | 1626.4   | 1588.5   |
| <b>CANADIAN DOLLAR</b> (9/6)           | 1.34        | 1.34     | 1.37     |
| <b>MEXICAN PESO</b> (9/6) <sup>3</sup> | 6.240       | 6.298    | 3.396    |

Sources: Major New York banks. Currencies expressed in units per U.S. dollar except for British pound in dollars



# This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

**BusinessWeek** **ONLINE**

## Sunday

Talk about this week's Cover Story with BW's John Byrne and Jack Stack of Springfield ReManufacturing—one of the companies that do their job so well other managers flock to visit and learn. **Sept. 10 9 p.m. EDT in the Globe**

## Monday

Windows 95 vs. the Mac: Join a debate between authors Dan Gookin (*Real Life Windows 95*) and Bob LeVitus (*Macintosh System 7.5 for Dummies*), plus Steve Wildstrom of BW's Technology & You. **Sept. 11 8 p.m. EDT in the Coliseum**

## Wednesday

Taking the "open" out of heart surgery: Heartport's revolution in bypass procedures. **Sept. 13 9 p.m. EDT in the Coliseum**

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event

For a free trial diskette including 10 free hours on AOL, call 1-800-641-4848 and mention Business Week.



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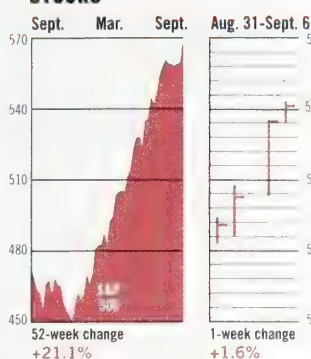
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# Investment Figures of the Week

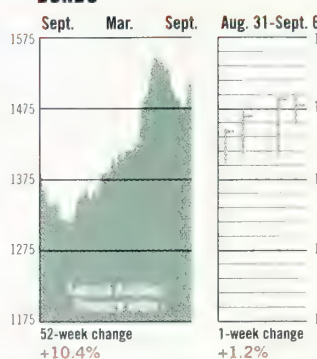
## PRIMARY

Interest-rate cut in the off-  
 ings are betting the signs  
 ness in the economy will  
 Federal Reserve to low-  
 er this month—a big  
 icks. The Dow industri-  
 above 4683 on Sept. 6,  
 level in nearly four  
 the most dramatic ac-  
 the broader indexes:  
 0, the S&P MidCap 400,  
 sell 2000 all made new  
 ed in large part by re-  
 nith in technology

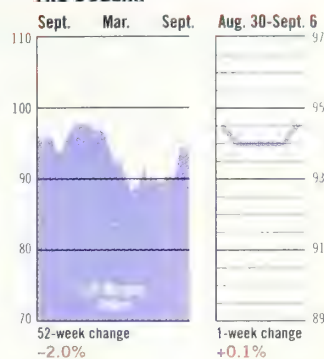
## STOCKS



## BONDS



## THE DOLLAR



## STOCK ANALYSIS

| STOCKS                       | Latest | % change<br>Week | % change<br>52-week |
|------------------------------|--------|------------------|---------------------|
| INDUSTRIALS                  | 4683.8 | 1.7              | 20.5                |
| COMPANIES (S&P MidCap Index) | 215.4  | 2.8              | 21.7                |
| PANIES (Russell 2000)        | 310.6  | 2.4              | 20.9                |
| NIES (Russell 3000)          | 329.4  | 1.9              | 21.6                |

| STOCKS              | Latest   | % change (local currency)<br>Week | % change<br>52-week |
|---------------------|----------|-----------------------------------|---------------------|
| FINANCIAL TIMES 100 | 3557.7   | 1.5                               | 11.0                |
| NIKKEI INDEX        | 17,620.4 | -2.0                              | -12.0               |
| EURO COMPOSITE      | 4572.1   | 0.9                               | 5.4                 |

## FUNDAMENTALS

|                              | Latest | Week ago | Year ago |
|------------------------------|--------|----------|----------|
| 90-DAY TREASURY BILL YIELD   | 5.48%  | 5.44%    | 4.65%    |
| 30-YEAR TREASURY BOND YIELD  | 6.59%  | 6.69%    | 7.56%    |
| S&P 500 DIVIDEND YIELD       | 2.37%  | 2.40%    | 2.70%    |
| S&P 500 PRICE/EARNINGS RATIO | 16.4   | 16.2     | 18.7     |

## TECHNICAL INDICATORS

|                                           | Latest | Week ago | Reading  |
|-------------------------------------------|--------|----------|----------|
| S&P 500 200-day moving average            | 508.8  | 506.7    | Positive |
| Stocks above 200-day moving average       | 76.0%  | 74.0%    | Negative |
| Speculative sentiment: Put/call ratio     | 0.53   | 0.60     | Negative |
| Insider sentiment: Vickers sell/buy ratio | 2.35   | 2.39     | Neutral  |

BLOOMBERG FINANCIAL MARKETS

## INDUSTRY GROUPS

| INDUSTRY GROUPS              | % change<br>1-month | % change<br>12-month | Strongest stock in group | % change<br>1-month | % change<br>12-month | Price  |
|------------------------------|---------------------|----------------------|--------------------------|---------------------|----------------------|--------|
| TELECOMMUNICATIONS EQUIPMENT | 11.7                | 68.9                 | CISCO SYSTEMS            | 25.6                | 174.6                | 68 3/4 |
| OIL & GAS DRILLING           | 10.2                | 10.7                 | ROWAN                    | 17.5                | 11.7                 | 8 1/8  |
| HEALTHCARE SERVICES          | 9.9                 | 31.3                 | AMGEN                    | 16.9                | 80.8                 | 48 7/8 |
| BANKING & FINANCIAL SERVICES | 9.9                 | 36.5                 | HOUSEHOLD INTERNATIONAL  | 10.4                | 46.0                 | 57 1/8 |
| TELEPHONES & TELECOM         | 8.6                 | 6.9                  | CHRYSLER                 | 15.1                | 17.8                 | 57 1/8 |

| INDUSTRY GROUPS          | % change<br>1-month | % change<br>12-month | Weakest stock in group     | % change<br>1-month | % change<br>12-month | Price  |
|--------------------------|---------------------|----------------------|----------------------------|---------------------|----------------------|--------|
| ENTERTAINMENT            | -4.2                | 22.3                 | KING WORLD PRODUCTIONS     | -8.3                | 1.3                  | 38 1/8 |
| TOBACCO                  | -4.1                | 17.7                 | INTL. FLAVORS & FRAGRANCES | -9.2                | 12.3                 | 47 7/8 |
| RETAIL APPAREL RETAILERS | -3.8                | -16.0                | THE LIMITED                | -6.1                | -9.5                 | 19 1/8 |
| PLASTICS & CHEMICALS     | -3.5                | 20.4                 | ENGELHARD                  | -9.7                | 54.2                 | 27 1/4 |
| PHARMACEUTICALS          | -3.1                | 15.2                 | BROWN GROUP                | -31.5               | -53.7                | 17 1/8 |

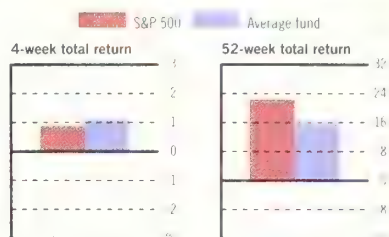
MOTIVATIONAL

## MUTUAL FUNDS

| MUTUAL FUNDS                | %   | LAGGARDS                              | %    |
|-----------------------------|-----|---------------------------------------|------|
| total return                | %   | Four-week total return                | %    |
| SELECT HOME FINANCE         | 9.5 | WRIGHT EQUIFUND-SPAIN                 | -6.4 |
| RG PINCUS JAPAN OTC         | 9.3 | AMERICAN HERITAGE                     | -5.8 |
| AN OCEANOGRAPHIC TECHNOLOGY | 7.2 | ROBERTSON STEPHENS DEVELOP. COUNTRIES | -5.7 |

| MUTUAL FUNDS                  | %    | 52-week total return                | %     |
|-------------------------------|------|-------------------------------------|-------|
| total return                  | %    | WRIGHT EQUIFUND-MEXICO              | -47.6 |
| AN COMMUNICATIONS & INFORM. A | 93.2 | BT INVESTMENT LATIN AMERICAN EQUITY | -36.6 |
| Y SELECT ELECTRONICS          | 92.0 | HERCULES LATIN AMERICAN VALUE       | -35.2 |
| SMALLER COMPANIES A           | 86.2 |                                     |       |



ORIGIN: CRAWFORD

## FIVE PORTFOLIOS

Points represent the  
 value of \$10,000  
 one year ago  
 portfolio

ges indicate  
 total returns



This page is as of market close Wednesday, Sept. 6, 1995, unless otherwise indicated.  
 Includes S&P 500 companies only; performance and share prices are as of mar-

ket close Sept. 5. Mutual fund returns are as of Sept. 1. Relative portfolios are valued as of Sept.  
 5. A more detailed explanation of this page is available on request. r= revised NA=Not available



## STAND AND DELIVER, CONGRESS

**I**t's crunch time in Washington. Congress is back, but can it perform? Inside-the-beltway pundits wonder if a "train wreck" between Democrats and Republicans over the budget will bring the nation to a financial halt. A far more important question is whether politicians of both stripes realize this may be their last chance to convince the public that the current two-party political system is worth saving at all.

Disenchantment with the November GOP "revolution" already has set in. Congress' approval ratings are way down, even below President Clinton's. In the heartland, people are beginning to ask what's really so different about Washington. Politicians continue to gorge on PAC money, lobbyists write their own legislation, political parties pander to extremists, and parochial legislators favor powerful local groups to get re-elected. General Colin L. Powell's nonpartisan popularity is inversely related to the country's political cynicism.

It's not too late. Start with the budget. The conservative radicals promised to kill entire government programs but then wimped out under pressure. Even after they are trimmed, farmers and ranchers still have their subsidies and the Appalachian Regional Commission still gets to build facilities at ski resorts. Government entitlement programs, like zombies, rise from the dead. There's still time to do the right thing.

Ditto for Medicare. Much of the GOP balanced budget is based on cutbacks in this program. But right now, Republicans are pretending that they can cut \$270 billion by giving every senior a choice: fee for service, vouchers, HMOs. Impossible. Instead of taking the hard political decision to shift Medicare recipients into managed-care programs, they are fudging the facts. The whole country is moving toward managed care. Congress should seize the moment and get it done now.

Congress looks better when it comes to tax cuts. A large amount of cuts, about \$250 billion, is substantial, and a capital-gains tax cut, expanded IRAs, and family tax relief are right on a pro-growth track. But proposing to give a credit to families with \$200,000 in income and penalize the working poor by chopping the Earned Income Tax Credit is simply the crassest kind of class warfare. It should be stopped now in conference.

Then there is regulatory relief. Pruning thickets of business regulation and tort reform to limit corporate liability are vital to the future health of the economy. Yet once again, extremist efforts to eliminate all government health-and-safety and environmental regulations feed public cynicism that politicians don't care for ordinary citizens, just powerful constituencies. Regulatory reform must be accomplished, thoughtfully. Only anarchists believe in no government.

There is still a chance for the Republican Revolution with a capital "R" to come off. The GOP deserves kudos for moving beyond the rhetoric of change and actually trying to force change through the bureaucratic morass that is Washington.

But the political sleaze factor gripping the government for the past 30 years remains, and the nation's citizens want an end to it. Fifteen of the top 20 fund-raisers in Congress are freshmen Republicans, gobbling up campaign contributions from vested interests. These same Republicans fight against eliminating federal subsidies and programs to protect their own local interests. It's business as usual for them.

Washington should take note. If it doesn't deliver the goods this time, the system could easily fragment. An independent challenge and third parties have a certain romantic appeal, but there's no way that fragmentation will end gridlock. Beware of three parties, or four, or...

## ECONOMIC NATIONALISM: DISASTER AHEAD

**W**hen Pat Buchanan and Jesse Jackson begin to sound like identical twins, it's time to listen. Despite their positions at the extreme wings of the Republican and Democratic parties, both men are voicing an economic nationalism that is increasingly crossing political boundaries. It is a message of populism and nationalism that is posited against the dominant economic ideology of globalism. Listen more closely to the rhetoric, and you'll detect a distinctly anticorporate bias.

To both the far right and far left, the main issue is who benefits? Who is benefitting from the expansion of market capitalism throughout Europe, Asia, and Latin America? It is a serious question and Corporate America can't simply dismiss it by chanting the mantra of free trade. Profits are performing too well and wages too poorly to get away with that politically for very long.

The simple solution for economic nationalists is protectionism: Raise tariffs, impose quotas, prevent corporations from moving capital and jobs overseas, and cancel treaties such as NAFTA. In this way, they believe, the U.S. would lock the benefits of its economic growth inside its borders.

We believe that this kind of behavior would immediately lead to a global trade war and economic depression. The solution to stagnant wages is to improve the skills of the workforce. It is not fashionable these days to talk about the socioeconomic responsibilities of the corporation. But in an era when private institutions increasingly are being called on to do well the things that government has done poorly, corporations should not try to escape their responsibility for the development of the nation's human capital. It is in their long-term economic self-interest. It is in their long-term political self-interest. And it is their civic duty.



## Don Vinegar

Don Vinegar doesn't have to paint that smile on – it's all his. He earned it by getting through a bout with cancer, not the kind of thing that usually leaves people whooping it up. But Don has left the problem so far behind, so completely behind, that he can only feel a little delirious.

is smiling on the inside too.

For one thing, his finances are fine. In plain language, AFLAC insurance helped stop his money from flowing out of his pocket through the holes in his health coverage. (What Don discovered is that AFLAC, being experts in this sort of thing, really made a difference.) He's fine. Life is fine.

So here you see Don, happy, healthy and over it. Hallelujah!

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# BusinessWeek

EMBER 25, 1995

A PUBLICATION OF THE MCGRAW-HILL COMPANIES

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# THE PRINCE

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At 38, Saudi Prince Alwaleed is one of the world's most powerful investors—with big stakes in Citicorp, Euro Disney, Four Seasons Hotels, The Plaza, and Saks. Canary Wharf may be next. His empire: \$10 billion—and growing.

An **EXCLUSIVE** look at how he operates BY JOHN ROSSANT

PAGE 85

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# BusinessWeek

SEPTEMBER 25, 1995

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He's like a Warren Buffett on a world prowl. Indeed, Saudi value investor Alwaleed has much more in common with the Sage of Omaha than with the glitzy petro-sheikhs of the '70s and '80s—and it shows in his portfolio of high-profile assets

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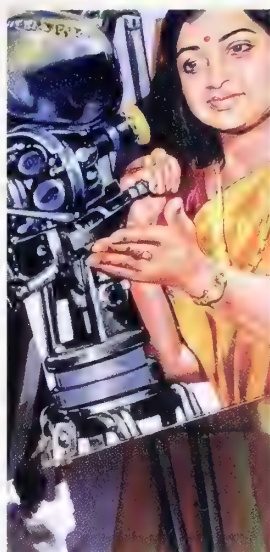
### PRINCE

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# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI



## CORPORATE SWEETS

### AN EMBARRASSMENT OF BANK DIRECTORS

WHEN CHEMICAL BANK AND Chase Manhattan Bank combine, 12,000 jobs will be axed. But the banks' directors can't complain. Outside board members from both banks will have spots. Result: The new bank will have 36 directors, becoming the second largest board in Corporate America, according to a review of proxies by the Directorship research group. Securities firm Bear Stearns (37) will remain No. 1.

Officials haven't yet figured out what to pay directors of what will be the nation's largest bank (assets: \$297 billion).

Bank analysts expect the pay package to use each bank's best features: Chemical's salary is higher (\$40,000 yearly, vs. \$25,000), and Chase has the richer annual stock award (500 shares, vs. 200). Why such a big board? "It will be a larger institution," says a Chemical spokesman, "and we will need them."

Not all agree. "This is unwieldy," says Alyssa Machold, deputy director of the Council of Institutional Investors. "It's hard to imagine them coming to quick decisions." Wall Street analysts say combining the boards was easiest politically. Banks tend to have large boards. By the Investor Responsibility Research Center's estimate, big companies' average board size is 12; for banks, 17. Citicorp, for now the largest bank, has 17. By 1997, Chase-Chemical plans to shrink its board size to 28 through retirements.

## THE LIST STADIUM SHOCK

Pro football ticket prices shot up 9.3% this season, to an average \$33.39. Worse, the prices have little to do with team quality. So we developed a Gridiron Value Index that relates ticket cost with each team's Vegas Super Bowl odds. The value leader is last season's champ, San Francisco, which boasts Jerry Rice. The worst value is an expansion team, the Carolina Panthers: It's 0-2 and has the fifth-highest ticket price.



REAL DEAL: '49ers' Rice

### WHAT YOUR GAME TICKET BUYS

| BEST VALUE    |            |                       |              | WORST VALUE |                       |
|---------------|------------|-----------------------|--------------|-------------|-----------------------|
|               | AVG. PRICE | GRIDIRON VALUE INDEX* |              | AVG. PRICE  | GRIDIRON VALUE INDEX* |
| SAN FRANCISCO | \$39.75    | 96.8                  | HOUSTON      | \$31.32     | 4.2                   |
| MIAMI         | 32.56      | 76.8                  | WASHINGTON   | 35.70       | 3.7                   |
| DALLAS        | 38.25      | 65.4                  | ST. LOUIS    | 33.61       | 2.9                   |
| PITTSBURGH    | 30.71      | 54.3                  | JACKSONVILLE | 35.00       | 0.6                   |
| NEW ENGLAND   | 34.22      | 41.7                  | CAROLINA     | 37.92       | 0.5                   |

\* Ticket price divided into current odds of winning the Super Bowl

DATA: TEAM MARKETING REPORT LAS VEGAS HILTON SUPERBOOK, BUSINESS WEEK

**TALK SHOW** "Ten years ago, we killed off their ma. Now, let's finish off her seven little bastards."

—Timothy Price, president of MCI's long-distance division, firing up the sales force for possible competition from Baby Bells

## POLITICS AS USUAL

### PACs: WHAT A DIFFERENCE A SWEEP MAKES

REPUBLICANS HAVE LONG griped that political donations from business tilted toward the Democrats. Since the GOP took over Congress, though, things are different. The National Republican Congressional Committee reports that the richest 400 political action committees gave overwhelmingly to GOP House candidates during 1995's first half—\$10.1 million, or 58% of the total.

During the 1993-1994 election cycle, the same PACs gave 65% of their money to House and Senate Democrats. Last time, the American Hospital Assn. gave two-thirds of its boodle to the Dems. Now, this is down to a mere 20%. The group says it's unaware of its partisan shift and makes donation decisions by

individual merit. Says Representative Bill Paxton (R-N.Y.), NRCC chairman, of the PAC switchers: "They felt they had to give their money to the Democrats, but now they've been liberated."

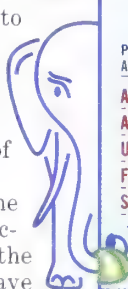
While such longtime Democratic backers as labor have stayed

### TOP FIVE PACs GOING REPUBLICAN

| POLITICAL ACTION COMMITTEE     | SHARE OF MONEY TO GOP CANDIDATES 1994* |
|--------------------------------|----------------------------------------|
| AMERICAN HOSPITAL ASSN.        | 32.6%                                  |
| AMERICAN MEDICAL ASSN.         | 56.6%                                  |
| UNITED TRANSPORTATION UNION    | 3.6%                                   |
| FEDERAL EXPRESS                | 30.4%                                  |
| SEAFARERS' INTERNATIONAL UNION | 10.6%                                  |

\*ENTIRE 1994 ELECTION CYCLE TO BOTH SENATE AND HOUSE CANDIDATES  
\*\*FIRST HALF OF 1995, TO HOUSE CANDIDATES

DATA: NATIONAL REPUBLICAN CONGRESSIONAL COMMITTEE



true, there are desertions. The United Transportation Union, which gave little to the Republicans before, now sends them almost half its largesse. Some Republicans, say union lobbyist J.M. Brukenhoefer, "understand the issues." Mary Beth Regan

## SLUGFESTS

### FLIPPER, COVER YOUR EARS

JACQUES COUSTEAU IS DIVING into the murky waters of a nasty family feud. The famed oceanographer, now 85, charges that his son, Jean-Michel, is cashing in on the family name to promote a business venture—the posh new Cousteau Fiji Islands Resort. The elder Cousteau filed suit Sept. 4 in Fiji

reputation and that of the Cousteau Society, a nonprofit foundation. Another defendant is one of Jean-Michel's investors, resort-owner Po Ranch, whose manager, Larry Callahan, says Jacques is being "unfair."

Cousteau père, who lives in Paris and has just completed a documentary about Danu



THE COUSTEAUS: At war

to force Jean-Michel, 57, to drop the family name from his \$3 million resort or print a disclaimer wherever it appears on stationery or promotional material. Jacques claims the name damages his

River pollution has had stormy relations with his son for years, friends say. Jean-Michel, recalling how he has worked closely with

dad on past documentaries, refuses to budge on the sort-name issue. He says in a statement: "I am proud to be a Cousteau, and I am proud of my father's accomplishments." Eric Schatz



With Fidelity's 401(k), we went from zero to 90% participation. The other 10% are probably hoping to hit the jackpot."

*Jessica Wasner, Office Manager, Desktop Data*



**H**aving a great product doesn't mean people will automatically buy it. To accomplish that takes something more. To Desktop Data, a developer of news processing software, that something more was Fidelity's approach to 401(k) plans – an integrated and coordinated service, all under one roof and only available directly from Fidelity.

"From day one, The CORPORATEplan for Retirement was great," said Desktop Data's Office Manager, Jessica Wasner. "Getting the plan started was an absolute breeze. I had no idea it would be as easy as it was."

So, your people had no trouble understanding what the plan was all about? "Not a bit. They're bright people. Software professionals. Even so, financial stuff can be mystifying. But Fidelity's people were great. They explained everything in simple terms – without talking down to anyone. Of course, their enrollment and communications materials are great, too."

And all that made a difference? "90% participation right off the bat. I'd say, yes, a big difference. Wouldn't you?"



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# Up Front

## PAPER PLAYS

### IT'S QUIET... TOO QUIET... BUY!

HERE'S ONE CLEVER WAY TO arbitrage takeover candidates in today's hot merger market: Look for an absence of trading by corporate insiders. Not wanting to draw the unwanted attention of federal regulators, insiders usually refrain from buying or selling their company stock while a deal is cooking.

Recent example: Chase Manhattan, due to be acquired by Chemical Banking. According to Fort Lauderdale (Fla.) research firm CDA Investment Technologies, the last time a Chase officer made a major sale—90,000 shares by John Scicutella, an executive vice-president who left to join Prudential—was in the spring.

What are the best pros-

pects? CDA has come up with several by finding companies whose insider moves have stopped and whose stock is up, as if to signal a pending deal. Only Riverwood, a paperboard maker that went public in 1992 and is 81.5%

owned by Manville, admits it is exploring going on the block. Shelby Williams, which makes seating, says it has had no offers. Hibernia, busy gobbling up smaller banks

around New Orleans, attributes its lull in insider activity to an end of execs' routine portfolio adjustments.

CDA readily admits its method is hardly infallible. Insider activity may cease for a number of personal reasons unrelated to the deal mill. □

| Takeover Signal?                      |      |
|---------------------------------------|------|
| Last Significant Insider Sale         |      |
| <b>HIERNIA</b>                        | 1994 |
| <b>RIVERWOOD</b>                      | NONE |
| <b>SHELBY WILLIAMS</b>                | 1994 |
| DATA CDA INVESTMENT TECHNOLOGIES INC. |      |

## SPORTS BIZ

### REINVENTING THE GLOBETROTTERS



**KAREEM:** *Loyal opposition*

THE HARLEM GLOBETROTTERS are making a comeback with the help of Kareem Abdul-Jabbar. The 69-year-old team, known for its courtside clowning and jazzy moves, has overhauled its format: To rebuild attendance, they now play serious basketball.

Their old foes, the hapless Washington Generals, used to

get well-scripted drubbings. For the Globetrotters' current European tour, the 7-foot-2 Jabbar, who retired from the Los Angeles Lakers in 1989, is leading a new opposition team of other former stars, such as Jo Jo White.

The Globetrotters won their first game 91-90 in Zurich Sept. 8 and drew 45,000. They say they will pay Jabbar up to \$500,000 for the European tour, ending in London Oct. 1.

Jabbar, 48, was enlisted by former Globetrotter Mannie Jackson, who bought the flagging team in late 1993 from International Broadcasting, then in bankruptcy court. Under Jackson, the team's yearly attendance surged 30%, to 2 million. Before, revenue was weak, with attendance down two-thirds from the early 1980s. One reason: NBA play has gotten a lot more showy and Globetrotter-like. □

**FOOTNOTES** This year's rise in assignments for search firms: to find directors, 43%; top executives, 32%; middle managers, 16%

## DRAWN & QUARTERED



## NEW WORLD ORDER

### THE NEXT RUSSIAN PURGE: WEAK BANKS

A SHAKEOUT IS ON THE WAY for Russia's fledgling banking system—which is plagued by fast-buck artists, greedy industrialists, and organized crime. By some estimates, up to 50% of Russian bank loans are now past due and, given the country's inadequate legal system, often nearly impossible to collect. The system's flimsy condition was highlighted recently when money markets ground to a halt. Reason: Bankers stopped lending to each other when a few of them failed to repay loans. The Central Bank solved the crisis by intervening to re-

vive the interbank lending market.

Nevertheless, the Central Bank makes clear it wants to drive out smaller banks with poor balance sheets. Even before the crisis, the Central Bank already had closed 5 insolvent small banks—and predicts 100 more will close soon. It started squeezing the banks earlier this year

by quadrupling the amount of money they must set aside

reserves. Western analysts applaud this hard line.

The Central Bank faces a tricky task: With the parliamentary elections looming

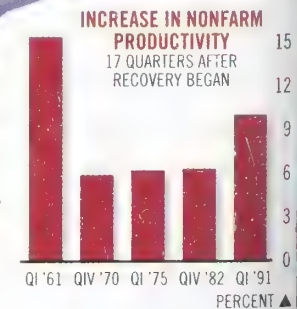
in December, the government doesn't want to be embarrassed by a string of banking failures. The great Russian banking showdown is far from over. *Patricia Kras*



## THE BIG PICTURE

### PRODUCTIVITY'S POWERFUL PACE

The current economic expansion's productivity increase outdoes those of the three previous recoveries. Only the booming 1960s look better. Reasons for the 1990s pace: no significant slowdowns in mid-recovery, big-time cost-cutting, and better technology.



DATA: BUREAU OF LABOR STATISTICS





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## 3-D: WHAT HAPPENED TO APPLE?

How could you possibly have written "3-D Computing" (Cover Story, Sept. 4) and not mentioned Apple Computer Inc.? Apple recently shipped QuickDraw 3D for its Power Macintosh computers—the only personal-computer company to include 3-D with its computer systems and operating-system software. Applications for it will be available in a few months—not years, as with the Intel-Microsoft platforms. Instead, you list Microsoft Inc. as a "major player" in the area, despite the fact that they have yet to ship a product.

Joe Marini

Principal, Lepton Technologies  
San Francisco

As I was reading your article on 3-D computing, I noticed there was no mention of Apple Computer and the Macintosh. Macs have played a big role in 3-D computing. Animation created on them has appeared in places ranging from the Intel Pentium commercials to Enterprise B in *Star Trek: Generations*. PowerPC chips are roughly 30% faster than Pentium chips of the same clock speed for "floating point" calculations, which are essential to 3-D rendering. And Apple's freely available QuickDraw 3D aims to create a standard for 3-D file formats, as with QuickTime movies. Now, Power Mac users can rotate and view 3-D models in as simple a program as ScrapBook—and then drag-and-drop it into a text editor. Let's see Windows 95 do that!

Vijay Iyer  
Baldwin, N. Y.

## KUDOS AND CAUTION FOR HOSPITAL TAKEOVERS

In "Balance sheets that get well soon" (The Corporation, Sept. 4), you seem to give every reason for Colum-

bia/HCA Healthcare Corp.'s success except one: excellent customer service. Recently, my wife was afflicted with terrible abdominal pain on a Saturday evening. Experience had told us that, we were to visit our nonprofit local community hospital, we could expect wait of at least an hour and probably more. Needing immediate attention, we turned to the emergency room at Columbia Doctor's Hospital. We arrived at 7 p.m. By 7:15 p.m., my wife had been seen by her physician, had her blood drawn, and had been advised that an appendectomy was in order. The anesthesiologist and surgeon were summoned from home, and within 30 minutes she was in the operating-prep area. During the whole process, I was dumfounded by the courtesy, speed, and efficiency of the staff.

## CORE COMPONENT

"Apple recently shipped QuickDraw 3D for its Power Macintosh computers—the only PC company to include 3-D with its computer systems"

I suppose others may continue to utilize the services of the nonprofits in our community. There, they can enjoy a less surely wait while the physician's services are consumed by Medicaid patients who use the emergency room for the after-hours clinic to treat runny noses and common colds. As for me and my family, we will vote with our wallet and enjoy the services of the Columbia facility. It may cost us more, but when we purchase a premium product we don't mind paying a premium price.

Bruce W. Holste  
Little Rock  
Towerbull@aol.com

Your article possibly inadvertently portrays the true nature of health-care industry takeovers. There were eight



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statements about cutting costs for the company, but no mention of lower costs for the patients.

Vincent F. Guinee, M.D.  
Houston

## OUR CUSTOMERS ARE NOT 'POTENTIAL DEADBEATS'

In "Nothing sub-prime about these profits" (Finance, Sept. 4), your characterization of our customers as "potential deadbeats" is both callous and offensive. Among our borrowers are laid-off workers, retirees, divorced mothers, and entrepreneurs—the majority of whom are trying in earnest to improve their financial situation. We make money at what we do because we do it well, but that hardly constitutes "a step above loan sharking"—now or ever.

The juxtaposition of my "balance sheet" with that of our customers' only propagates damaging misconceptions about our business, as does the insinuation that Aames wants people to abuse the credit system. Lucky for us, we have worked hard for 42 years to build credibility and overcome the careless arrows slung at our profession.

Gary K. Judis  
Chairman and CEO  
Aames Financial Corp.  
Los Angeles

## THE U.S. HAS HAD THIRD PARTIES ALL ALONG

How come your story on third parties, "In '96, three may not be a crowd" (News: Analysis & Commentary, Sept. 4), dealt only with party-less individuals and ignored an already established third party? Not only does the Libertarian Party already exist, but it's the only party that responds perfectly to the country's current longing for less government, more personal liberty, and responsibility in both the social and economic arenas. Apparently, you don't consider the Libertarian Party as newsworthy as media luminaries like Ross Perot and General Colin Powell. But if 40 million Generation Xers vote Libertarian, you will.

Alan M. Perlman  
Highland Park, Ill.

Your article overlooks some important and relevant history. You assert that the two-party system in this century went "virtually unchallenged—until the last 25 years." This overlooks the alternative party bid of Teddy Roosevelt in 1912 as well as those of Henry A. Wallace and Strom Thurmond in 1948. In both years, these parties significantly affected the outcome of the election (Roosevelt came in second) and mani-

## CORRECTIONS & CLARIFICATIONS

"Bell Atlantic: Playing chicken on the I-way" (News: Analysis & Commentary, Sept. 4) should have made clear that the 40% pay cuts do not apply to all I-way workers, only to those who perform work at customers' houses.

festated deep problems in the politics of the time. If we think "politics is broken" now, then all the more need for us to learn the lessons of history.

Henry J. Grantges  
Washington

## A NASTY SIDE EFFECT TO CUTTING-EDGE SURGERY?

You report that the new "port-access" open-heart-surgery technique is likely to lower costs for insurers and employers ("Bypassing the trauma," News: Analysis & Commentary, Sept. 4). While that may be true for the individual case, we need to ask whether costs will increase overall: The volume of procedures may grow because the new technique is easier for the patient. Several recent studies on newer, less invasive procedures for gall bladder surgery have shown that costs overall rose due to such volume increases.

Rene H. Reixach  
Finger Lakes Health  
Systems Agency  
Rochester, N. Y.

## HOW TO LIVE LONG AND PROSPER IN CYBERSPACE

If the Internet is to become the marketplace of the Information Age ("The net as free-market utopia? Think again," Economic Viewpoint, Sept. 4), it will not simply be the digital replacement of yellow pages, newspaper ads, TV commercials, or even home-shopping channels.

To prosper in cyberspace, one must be able to demonstrate genuine value added—for example, in the form of sound advice, technical support, or expert opinion—all as free information. It will not take long for consumers to turn away from conventional retailers with hollow, if not misleading, sales pitches to vendors who can provide the knowledge for educated choices online. In this sense, there is no essential conflict between the cultures of free information and free-market capitalism.

James K. Ho  
Professor  
Information & Decision Sciences  
University of Illinois  
Chicago

## ACCEPTING THE RISK OF BREAST IMPLANTS

Your story leaves me cold ("A breast implant deal comes down to the wire," Legal Affairs, Sept. 4). Breast implants are not a medical necessity or even a medical recommendation: They are the result of a voluntary decision. If there are certain consequences as a result of that decision, those consequences are those of the individual alone. No one else made the decision, and no one else should be liable for any risk.

Carl Otter  
Atherton, Cal.

## WHY PAY FOR PERFORMANCE WON'T MAKE THE GRADE

Your article "Bad marks for pay-by-results" (Economic Trends, Sept. 4) is amusing indeed. Is there anyone who really thinks that a test program that uses performance-based incentives to compensate teachers, and that is implemented by educators, has a chance of working?

The current calcified and inflexible infrastructure of America's education system evolved over many decades under the leadership of people who, for the most part, believed that there was something inherently wrong with competition and monetary reward for performance in the classroom. Change the management team and the structure of each school system, develop a community culture that is based on solid teaching criteria over time, and maybe then teachers and parents will begin to have more confidence in performance-based compensation.

Craig A. Cuddeback  
St. Louis

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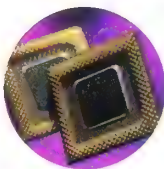
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## FRIENDS IN HIGH PLACES

The Rise and Fall of Clark Clifford

By Douglas Frantz and David McKean  
Little, Brown • 450pp • \$24.95

# THE GRANDDADDY OF INFLUENCE PEDDLERS

For two generations, Clark McAdams Clifford personified the Washington Establishment. He was Harry Truman's adviser, John Kennedy's lawyer, Lyndon Johnson's Defense Secretary, a confidant to powerful senators, and the capital's most sought-after corporate attorney. So when his reputation was shattered by a scandal involving the Bank of Credit & Commerce International during the early '90s, Washington was understandably shocked.

Now, the mystery of why Clifford's career came to such ruin has been solved. *Friends in High Places: The Rise and Fall of Clark Clifford* details how an ambitious man's pursuit of power, prestige, and money can run amok when his capacity for self-delusion is great enough. *New York Times* reporter Douglas Frantz and David McKean, an aide to Representative Joseph P. Kennedy II (D-Mass.), play objective reporters in an exhaustively researched biography. But

fair as they are, they paint an unflattering portrait of Clifford—and the influence-peddling industry that he spawned. Indeed, Clifford was the prototype for the modern-day lobbyist. "He reshaped the way lobbying worked in the nation's capital, making it respectable and even desirable to trade quietly on relationships with government officials while telling clients with a straight face that he had no influence," Frantz and McKean write.

Today, Clifford's approach is known as the revolving door: Work in a high post and then cash out for millions as a "consultant." The key is convincing everyone—including yourself—that you're honorable and that your clients' inter-

ests and your own coincide with those of the nation. As the authors report: "Clifford believed it was his definition of what was right that counted."

For example, as President Truman's White House counsel, Clifford took credit for plotting Truman's startling upset of Thomas Dewey in 1948. Only decades later, after he had prospered as the widely credited mastermind of that victory, did Clifford confess that the campaign's strategy had been the brainchild of James Rowe, a former aide to President Franklin D. Roosevelt.

Another troubling story: Over a period of many years, Clifford lent several thousand dollars to his close friend, Supreme Court Justice William O. Douglas. Yet Clifford saw no conflict in arguing a corporate client's case before the court. Today's ethics laws bar such financial entanglements.

Then there are dozens of cases in which the superlawyer used his government contacts to win favorable regulatory rulings or tax breaks for the likes of Howard Hughes, Phillips Petroleum, the DuPont family, and Knight-Ridder. Yet he would insist to each client that he did not wield "any influence of any kind" in Washington.

Surely Clifford was fooling only himself. His stature continued to grow along with his legal victories, thanks to another Washington art form he invented: press spin. Starting in his White House days, Clifford would cultivate close relations with influential journalists, feeding them political tidbits as an anonymous source and winning glowing press coverage in return.

But then Clifford overreached. In the late 1970s, he agreed to help BCCI ac-

quire an American bank, Financial General Bankshares of Washington. BCCI, headquartered in Luxembourg, was a shadowy bank founded by a Pakistani banker, and it would later be accused of laundering drug money and aiding unsavory characters ranging from Palestinian terrorist Abu Nidal to Panamanian strongman Manuel Noriega. When federal regulators blocked the acquisition, Clifford spent four years engineering Financial General's takeover—ostensibly by a group of Arab investors, with BCCI acting only as a paid consultant. The sale went through in 1982, after Clifford gave his word that BCCI had no direct investment in the bank. He was rewarded with the bank's chairmanship, and over the next 10 years Clifford and his law partner, Robert Altman, received \$40 million in fees for rigged stock sales—all financed by BCCI.

After word broke that BCCI was the real owner of the bank, Clifford and Altman were indicted in New York for lying about the arrangement. Clifford never stood trial because of a heart ailment, and Altman was acquitted because the prosecution had no smoking gun that proved he and Clifford knew BCCI secretly owned Financial General. But Frantz and McKean make a convincing case that, at the very least, Clifford had to suspect the truth.

On two counts, the book falls short. The writing is long-winded and flat. We are reminded endlessly, for example, that Clifford is tall and handsome and that he stole credit for Truman's election. The more serious weakness: The authors take us to the water's edge and then stop. Was Clifford a liar or a dup in the BCCI affair? They don't render a verdict, citing no "conclusive" evidence. Readers will have no trouble making up their minds: \$40 million will prompt anyone to look the other way.

Clifford's downfall is a tragic reminder that greed clouds the judgments of the most distinguished figures. His tale also reveals a sadder truth. Washington is home for all too many high-powered Clark Cliffords who win plaudits from statesmen even as they're exploiting public service to accumulate private wealth. And despite his comeuppance, Clifford is still their role model.

BY OWEN ULLMAN

Ullmann is *BUSINESS WEEK's* senior news editor in Washington.

## FRIENDS IN HIGH PLACES

## THE RISE AND FALL OF CLARK CLIFFORD

DOUGLAS FRANTZ & DAVID MCKEAN



BY CULTIVATING KEY JOURNALISTS,

CLIFFORD VIRTUALLY INVENTED PRESS SPIN



"Give me a way to see problems before  
they become problems."

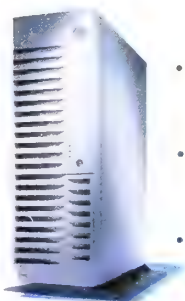


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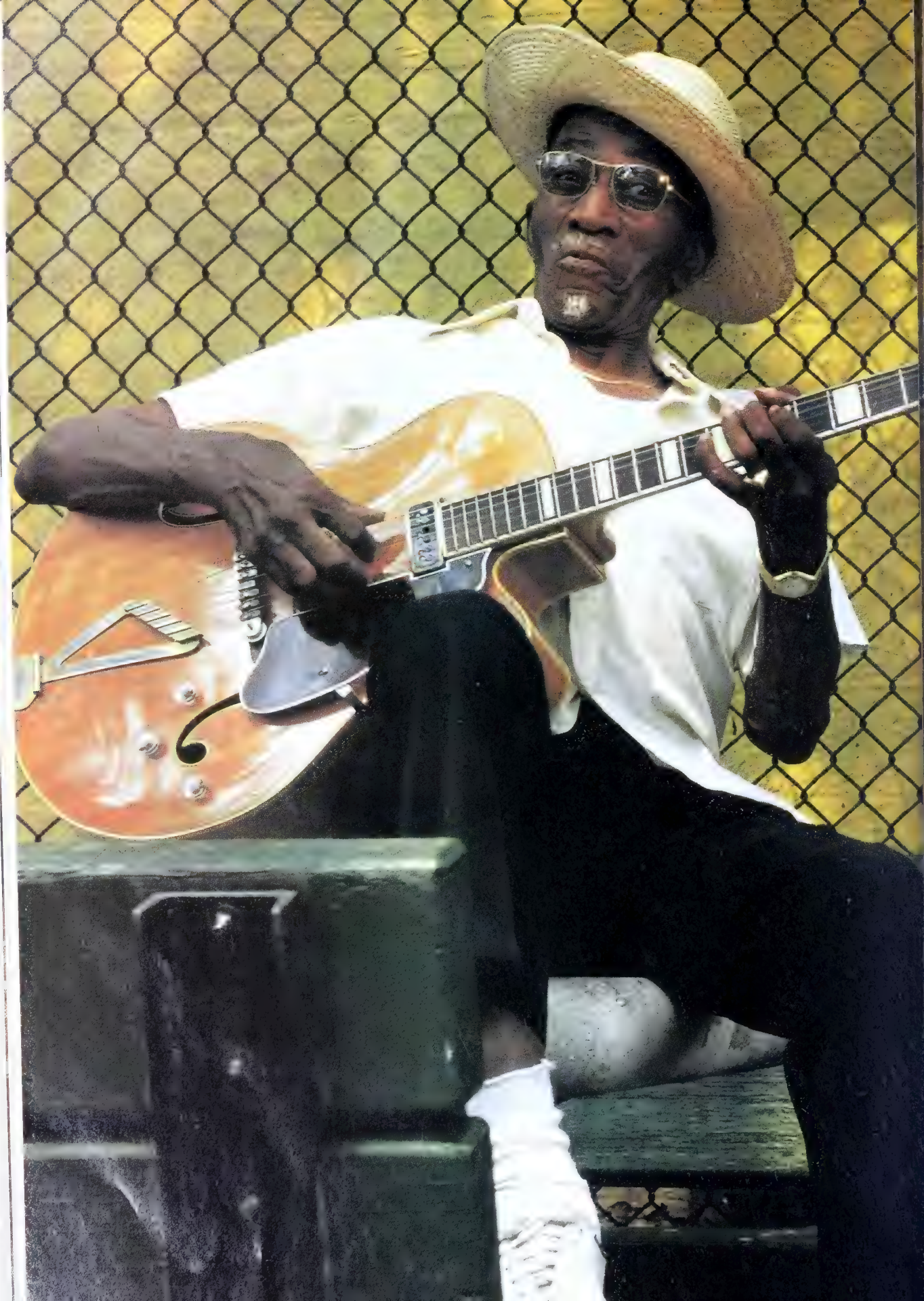
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*"After a while, nothing helped my knees.  
I had to have something done."*

WALTER J. PERRY  
NEW YORK, NEW YORK

Walter "The Buzzard" Perry says he was born to be a songwriter. In fact, he carried his guitar with him on the Italian front during World War II and serenaded his platoon. But 15 years ago, he started singing a different kind of blues.

It all began with an aching and swelling in his knees. Some days he couldn't stay at work, the pain was so bad. He even fell in the street and couldn't get up on his own. "I just stayed at home—shut in," he remembers. "It was awful."

Today, thanks to medical technology developed at Pfizer, Walter has two new artificial knees, and he's mobile again.

We're committed to finding cures. Even when the research takes over a decade, we take the time. We have to. It's for people like Walter.

"Now I can go anywhere I want to," he said.  
"I feel good."



*We're part of the cure.*



BY STEPHEN H. WILDSTROM

## SOFTWARE THAT'S TAILOR-MADE

**H**ow is software like a steam engine? At the Smithsonian Institution, there's a huge 1876 engine: beautiful, mechanically perfect—and on the brink of obsolescence the day it was built. Within a few years, steam gave way to smaller, more efficient internal-combustion engines and electric motors.

Like this mechanical marvel, today's software packages, such as Microsoft Office and Lotus SmartSuite, may be near the end of an evolutionary line. These programs seem to do everything and do most things well. But there are drawbacks: My installation of Office for Windows 95 fills 60 megabytes of disk space. Much of that space goes for options that a tiny minority of people use, such as indexing in word processors and regression analysis in spreadsheets. One result is a clutter of options that can make the programs harder to use.

**CUSTOM PACKAGE.** Before too much longer, you may be using an assortment of much smaller applications tied together into a package customized to your needs. For example, you might be able to combine a simple text-editing module with a spell-checker, thesaurus, and other tools to roll your own word processor. "That's what the future will look like," says Jeffrey Anderholm, director of product marketing at Lotus SmartSuite.

A new product for Win95, called OfficeBlox from AlphaBlox (800 227-2569), gives a glimpse of this new world. The \$70 product consists of little programs that are designed to augment rather than replace your existing applications. For example, jotting down a phone message in a conventional application requires saving the information as a file. The NoteBlox mini-app lets you type the note, then stick it anywhere—including your desk-



top—like a Post-it note. Instead of firing up a spreadsheet to crunch some numbers, you can use any of a dozen specialized business, financial, or scientific calculators provided by CalcBlox, then paste the results into documents. Other "Blox" can manage lists of information and provide an easy way to sort and classify your files. And additional modules are on the way.

AlphaBlox relies on a technology called object linking and embedding (OLE), which allows the easy sharing of data among applications. For example, if you used Calc-

Blox to calculate a number you pasted into your report, just click on the number, and the calculator will pop back up. While OLE has been around for several years, Windows 3.1 had a nasty tendency to crash if you linked more than a couple of programs. OLE is far more stable with Windows 95—and it's even more so with Windows NT and OS/2. Apple Computer is leading an effort called OpenDoc, which would create a common linking standard for different hardware and software.

A lot of work must be done before a collection of modules will replace, rather than augment, today's big applications. For one thing, using the modules will be confusing unless they share similar menus, icons, and buttons and unless they behave in similar ways. And competitors don't much trust Microsoft to make it easy on its rivals. "Will the company driving the de facto standard drive it to its own advantage?" asks Lotus' Anderholm.

Microsoft is ambivalent. Although modular applications are technically possible, says Dennis Tevlin, group product manager for Microsoft's best-selling Office Suite, it's not clear how profitable they would be. Customers, he says, want less complexity, but it's often tough to figure out whether that means programs with fewer options or with more choices offering point-and-click convenience.

Microsoft and Lotus have just revamped their suites, and a new version of Novell PerfectOffice is due this fall. The monster applications are probably good for one more overhaul. But like the museum steam engine, it may be the final perfection before extinction.

## BULLETIN BOARD

### SOFTWARE

#### FILE TRANSFER

Several readers responded to my Aug. 28 column, "Easing the pain of an upgrade," by suggesting that a tape backup can facilitate the job of moving files from an old com-



One option: The Conner parallel port tape drive

puter to a new one. It can help but won't do all the work. The tape drive can save time. First, copy files from your old hard drive to tape. Then, install the files on your new machine, either by using a compatible tape drive or by moving the same tape drive from one machine to another. The hitch involves Windows programs, especially if you have customized touches that you want to move to your new machine. You will have to reinstall many Windows programs for them to work properly. The process is trickier if you are moving to a machine with Windows 95 installed.

### THE WEB

#### CLICK AND FIND

For an easier way to search the World Wide Web, take the advice of reader Tom Wruk in Belvidere, Ill.: Use a one-stop service called Starting Point (<http://www.stpt.com>). Starting Point includes links to all the directory and search tools mentioned in my Sept. 11 column and a few more to boot. It also offers pointers to an assortment of interesting sites around the Internet.



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**Comprehensive preventive care** with at least two dental exams and cleanings per year. Some plans don't include fluoride or sealants. Yours should. These treatments help prevent cavities, which brings down the cost of care.

**Flexibility in appointment scheduling.** Many insurers encourage their participating dentists to schedule "plan patients" as fill-in appointments. Your employee may have to take time off during the day to receive dental treatment or wait months to be seen. That's not only a problem for the patient, it costs you valuable employee time.

**Plans that allow patients to visit the dentists and specialists of their choice.**

Research proves that patients won't go to dentists they don't trust. So you wind up paying the premium for unused benefits.

**Emergency, weekend and holiday care.** A plan that doesn't cover the unexpected is of no benefit to you or your employees. The emergency that isn't taken care of immediately can cost you dollars in downtime.

**Broad therapeutic coverage.** A plan that covers crowns and bridges, braces and dentures and even root canals may cost somewhat more, but will be more satisfactory to all plan users. Make sure that limitations on this kind of care are not unrealistically severe. You'll get fewer complaints even though employee co-payments are higher

for these services than for preventive care.

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RUDI DORNBUSCH

## COMMON MONEY— OR FUNNY MONEY?



**NO GAIN:**  
Maybe a single  
currency  
is inevitable—  
at best,  
as a way for  
Italy and other  
economically  
troubled nations  
to cover up  
their fiscal disarray

**F**or some it is inconceivable, for others inevitable—a single European currency. Yet the dollar's rally and German rate cuts have relieved European Monetary System strains and revived a monetary flight of fancy—common money for Continentals.

To observers from across the Atlantic (or the Channel), Europe needs a single currency like it needs a hole in the head. If Europe cannot forge ahead with plans for political union, what's the point of a common currency? Regardless of this fact, prenuptial agreements to a communal marriage of the mark, franc, lira, etc., have already been signed, with the wedding date scheduled for 1999.

What is going on? The idea of Europe '92, the final stage in a single European market, was a shot in the arm for a region that needed one. Some Europeans hope that a common European money plays the same role, helping divert attention from high unemployment and poor economic performance. That is one of the reasons why common money will become a reality. It has various groups behind it: The banking community sees it as a business opportunity. Brussels bureaucrats are ready to claim credit for it. And a few countries need it badly to cover up their rotten fiscal situations. These are powerful but poor reasons for going ahead.

Clearly, the convergence criteria set earlier by the Bundesbank in terms of inflation or debt are not going to be met by most candidates. So the talk is of finding a more flexible approach. If the budget is off-target, well, just build in some commitments and deal with the problems later. The idea is to use the common-money community as a European therapy group.

**DEBAUCHERY.** That is the kind of agreement Italy would love. It would cover the fiscal mess with a veneer of eligibility to hard-money status. In exchange, Italy would help support France when it came to pleading the soft-money case. There is so much to be gained by France and Italy that irresistible pressure for one currency may already exist.

But why would the German bondholding public and inflation-wary German burghers accept the risk that their currency gets debauched? Well, they were never asked. Wisely for the officials, nobody ever thought of holding a referendum on that issue in Germany. Although there are elections on the way to '99, the German political parties all play the

European card. The banks are gung ho to cash in on the venture. In sum, what on rational grounds is inconceivable may already be a fait accompli.

In the meantime, there are, of course, some hard questions around which the shadowboxing will continue. One is already resolved: The new European Monetary Institute will be installed in Frankfurt, giving that city a new edge in European finance, especially as Britain is sure to keep its pound out of any Eurocurrency. The next is what to call the new money. Be sure that Germany gets the last word on this, trading off that precarious privilege for accepting Italy's deficits. The compromise is to call it a *gulden*; that way, at least the name will not be French. And then there is the question of where to draw the line: Italy, yes—but Greece, Portugal, and Spain? First class is full; perhaps there will be some coach seats for the underachievers.

**ALTERNATE SCENARIOS.** Just to play devil's advocate, is there any way the drive to a common money might yet fail? At least two come to mind. Both recognize that from here to 1999, none of the participants can hold their breath. The first possibility is that Italy just cannot make it—one day there will be elections, and the present game of pretend will end. Italy's overindebtedness and budget problems will reemerge.

If that happens, a European money will be reduced to just what we have now: a de facto, stable, though not fixed, Franco-German currency relation with everybody else flocking around. The other possibility? The dollar weakens, as it does with great regularity. When that happens, the franc comes under pressure, and France finds the resulting high interest rates and high unemployment unacceptable. This makes for a replay of the 1992 currency mess.

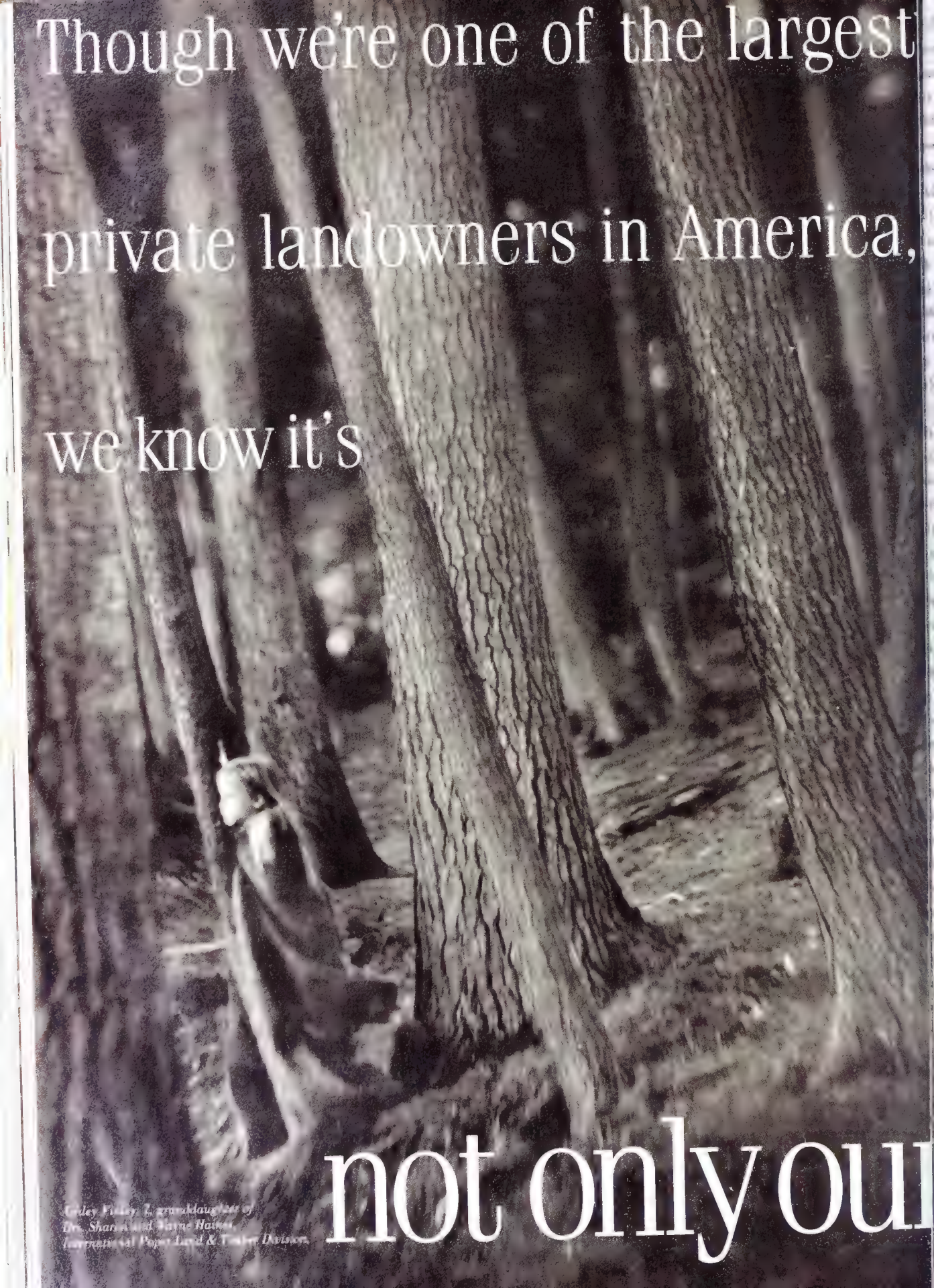
Europeans distrust U.S. skepticism of the idea of a common money. They blame it on an unwillingness of the U.S. to give up world money leadership, hegemony, and all that. Ten years ago, that might even have been a good story. By now, a new European money already looks defective and will hardly challenge the dollar.

It certainly will not help Europe restructure and solve its labor-market problems. Anyone who doubts that can look at German interest rates. Ten-year bonds offer a big premium. For good reason.

Dornbusch is professor of economics and management at Massachusetts Institute of Technology

KATHERINE JAMBERT



A black and white photograph of a forest. Several large, thick tree trunks are visible, leaning slightly. In the lower-left background, a person is standing, looking towards the camera. The lighting is dramatic, with strong shadows and highlights on the tree bark.

Though we're one of the largest  
private landowners in America,  
we know it's

not only our

*Grady Valley, a granddaughter of  
Doc, Sharon and Wayne Hatten,  
International Paper Land & Timber Division.*



## WHAT ARE THE ISSUES?

International Paper owns or manages over 6,000,000 acres of forestland in America.

With that ownership comes a responsibility to protect and care for this vast, renewable resource. We believe that a balance must be struck between land preservation and utilization.

We know there are millions of people who rely on our forestland for different yet important reasons. Some need lumber to build homes. Some need tons of paper to run their businesses. Some just want to go camping or fishing.

These are not complicated issues. But satisfying them involves complex personal, business and global issues.

If you're an environmentalist, you may ask how the ecology of our forest will be safeguarded so that wildlife will always have a thriving habitat. If you're a landholder, you may question whether International Paper will be growing, while maintaining resources, and providing recreation with more and better forests in the future. If you're a parent, you may wonder if your children and your children's children will always have forests in which to experience nature.

Deciding how best to use the land will be debated for centuries. At International Paper, managing the land better than we did it is an environmental and economic imperative because the success of our company depends much on the health of our forests as anything we do.

## WHAT WE ARE DOING.

Every year, we invest millions of dollars to find better ways to manage our land.

One result is a new, stronger family of pine trees. Developed through a process of natural selection, it produces more wood per acre over a 25-year growing period. We're planting 50 million of these "SuperTree" seedlings every year. By the year 2000, we'll have 30% more wood fiber growing on our lands than in 1990.

We've entered into partnerships with groups like The Nature Conservancy and The Conservation Fund, in addition to state and federal agencies.

Results? We're the first U.S. company participating in an inventory and protection program with the Department of the Interior's National Biological Survey. We already protect the habitats of 12 federally listed animals and one plant species on our lands. Of the land we own, 96% is available to the public through leasing and other programs for camping, hiking, hunting or boating.

## WHAT IT MEANS TO YOU.

Perhaps Theodore Roosevelt said it best: "The nation behaves well if it treats the natural resources as assets which it must turn over to the next generation increased, and not impaired, in value."

With this ad, we're beginning a dialogue that will raise issues and share viewpoints.

To talk further, please call Dr. Sharon Haines, Manager of Natural Resources, at 1-800-455-1046.

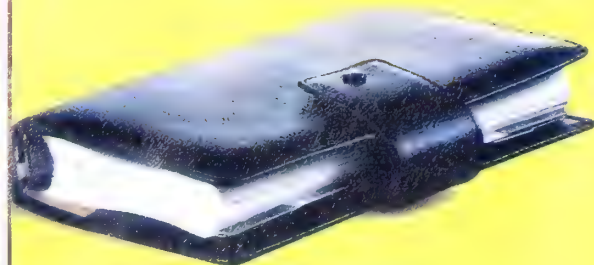
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1994



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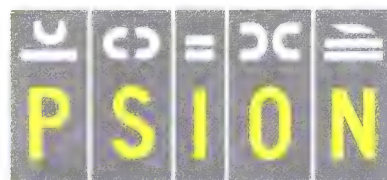
With a Pison Series 3a you can not only pocket all the information squeezed into bulging paper systems—you can also download data from your PC's wordprocessor, scheduler, spreadsheet and database ... and work on it anywhere, anytime, using its built-in software.

**Real power ...** No other palmtop matches the Series 3a's capabilities, versatility or performance. It's a powerful computer with windows, menus and icons as standard, **plus** the most advanced organizer functions around. But then, we did invent the idea (and have sold over one million worldwide). The latest Series 3a even has digital sound-bite recording, and there's an optional modem for fax, e-mail and on-line services.



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GENE KORETZ

## THE DOLLAR STILL HAS LEGS

Fundamentals thwart meddling

After its dramatic spurt over the past month or so, the dollar's appreciation may slacken for a while, warns economist Michael R. Rosenberg of Merrill Lynch & Co. But the direction for the greenback is still up, he says.

Among the possible hurdles facing the dollar, says Rosenberg, are a combination of global investors that their portfolios may be too heavily weighted in dollar assets, and the currency market's belief that the dollar's current

And Japanese investors, faced with increasingly low returns on financial investments at home and the fact that the yen's ascent has finally halted, will inevitably move more funds overseas.

## BYE-BYE, BANKERS

Ranks will thin and thin and thin

Only a few months ago, the long wave of downsizing plaguing U.S. labor markets seemed to be receding. Indeed, the consulting firm Challenger, Gray & Christmas Inc. notes that the 113,393 planned layoffs announced in the first four months of 1995 were less than half the year-earlier total.

Since then, however, the tempo has changed appreciably. Challenger reports that corporate job-cut plans unveiled from May through August hit 155,450—some 15% above the same period in 1994. The pickup in cuts seems to stem from the resurgence in mergers, particularly in banking. And it could escalate dramatically. A survey of leading bankers projects that job cuts in the industry will average some 90,000 jobs annually until the year 2000.

## UH-OH, DUELING JOB STATS

Gains may not be all that great

There's something odd about the signals being given off by the Labor Dept.'s two monthly employment measures. While the payroll survey indicates that employment is up a healthy 1.18 million since December, the household survey shows an increase of just 209,000—raising questions about the underlying strength of the labor market.

Most experts regard the payroll survey as the more reliable measure, since it is based on actual business records and is less volatile than the household survey, which is based on interviews with working-age people. But economist Christopher Low of HSBC Markets

points out that the household survey often picks up significant shifts in labor market conditions earlier than the payroll measure.

That's because the payroll stats include an upward adjustment for jobs created by business startups the survey doesn't catch. Since this adjustment is really just an educated guess, it can miss the boat if the economy shifts gears.

"The betting is that the current large discrepancy between the two measures will be resolved in coming months in favor of the payroll survey," says Low. "But until and unless that happens, the health of the job market will remain somewhat under a cloud."

## A D+ FOR DISMAL SCIENTISTS?

Even the Fed's gurus often goof

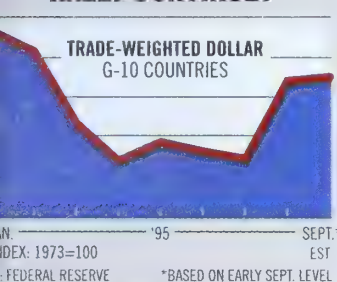
By all counts, the forecasts presented to Congress each February and July by the Federal Reserve Board's Federal Open Market Committee (FOMC) should be pretty darn good. After all, as economist Paul L. Kasriel of Northern Trust Co. observes: "The FOMC is theoretically in the unique position of being able to use monetary policy to influence the events it is projecting."

In the Federal Reserve Bank of Boston's *New England Economic Review*, economist Stephen K. McNees assesses the accuracy of FOMC forecasts from 1980 through 1994. The forecasts of key economic variables are presented in two forms: the range of projections issued by individual FOMC members, and the "central tendency" of such projections, which is the range without its high and low extremes.

What's the score? From 1980 through 1994, the final readings for real gross domestic product ended up within the growth ranges projected in February of those years only a third of the time. The success rates of the July GDP projections were just 19% for the full range of member forecasts and a fat zero for the "central tendency" numbers. That is, in no year did real GDP end up within the central tendency range projected by the FOMC in July of the same year.

To be sure, the study found that the FOMC did no worse than leading private forecasters as a group and actually did better in its inflation forecasts. Still, the results suggest that anyone who thinks the Fed has a firm grasp of the economy's current direction when it sets monetary policy had better think twice.

### WILL THE DOLLAR RALLY CONTINUE?



against the yen and the mark is steady at levels targeted by U.S., Japanese, and German monetary authorities. A third inhibiting factor is the recent rally in U.S. Treasuries, which has reduced real interest-rate differentials favoring U.S. investments.

For dollar partisans, the good news is that fundamental forces should overcome these hurdles in the months ahead. One thing, U.S. inflationary pressures seem to be subsiding, whereas wage growth, service-sector price pressure, and the weaker mark seem likely to boost German inflation next year.

Also, U.S. inflation expectations may be dealt a further blow if claims for the U.S. consumer price index states the actual inflation rate in action to revise the index and cut inflation-adjusted government outlays.

Even the deteriorating Japanese economy, Rosenberg also expects further dollar strength against the yen in the months ahead. The Bank of Japan's latest hike in its discount rate to a historic low of 5% underscores its awareness that the economy cannot recover without further monetary easing and a lower yen.

### TWO VIEWS OF U.S. JOB GAINS







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**F**rom his office in downtown Columbus, Ohio Governor George Voinovich couldn't see Cleveland with a telescope. But the governor can be forgiven an occasional glance toward the city he helped rejuvenate during his years as mayor there. Because Voinovich, now in his second term as governor, has used the same vision of business success that polished the rust off Cleveland's economic reputation as his model for running the state. The results have been impressive.

The state of Ohio once again leads the nation in attracting, keeping and developing business. For the second year in a row, *Site Selection* magazine's survey of business development in the U.S. ranked Ohio a strong number one, beating out even the traditional growth centers of the Sunbelt states. In 1994, Ohio's expansion activity added up to more than the combined total of 28 states (and the District Of Columbia) with a population of more than 125 million people.

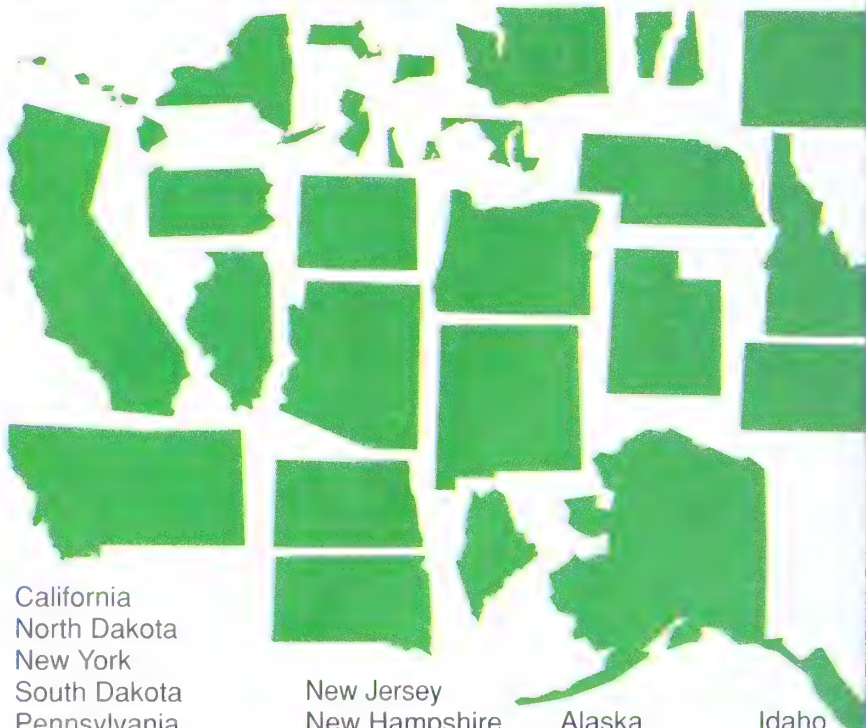
*"Ohio has a commitment to entering the 21st Century as a leader, not just in this country, but in the new arena of global business competition."*

*George V. Voinovich*



*Sound plan,  
government/business  
partnership, key  
to state's  
Success*

## 1994 EXPANSION ACTIVITY



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North Dakota  
New York  
South Dakota  
Pennsylvania  
Delaware  
Illinois  
District Of Columbia  
Massachusetts  
Maine

New Jersey  
New Hampshire  
Connecticut  
Rhode Island  
Colorado  
Vermont  
Arizona

Alaska  
Washington  
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Montana  
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The above states combined = **901** new and expanded corporate facilities

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Ohio is home to our corporate headquarters, research center, 13 plants in 8 different communities, and 8,000 valued associates. Over the past decade,

we have invested some six hundred million dollars in new and improved manufacturing operations in Ohio.

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# NORTHEAST OHIO'S ROCKIN' RENAISSANCE

## THE COMMUNITY BUILDS ON ITS REVITALIZED MANUFACTURING BASE AND EMERGING SERVICE AND TOURISM SECTORS

**H**ave you heard the news? Northeast Ohio's rockin' today. Architect I.M. Pei's jewel of a design for the \$92 million Rock and Roll Hall of Fame at last sparkles on the shores of the North Coast. The signature glass tent that soars 14 stories above Lake Erie stands as the most recent symbol of Northeast Ohio's equally inspiring renaissance.

Want a ticket to a Cleveland Indian's game? Forged about it! The Tribe now thrills soldout crowds at the state-of-the-sport Jacobs Field, part of the \$435 million Gateway sports and entertainment complex that represents one of the region's largest public-private economic development projects. In fact, the red-hot Indians' rise from the American League cellar to pennant contention neatly parallels the region's resurgence.

Yes, Virginia, the statute of limitations has expired on jokes aimed at Cleveland when its embattled downtown endured some down times during the '70s and early '80s. Today, the infamous inflammable Cuyahoga River has been reignited—this time with one of the most vibrant entertainment districts in the world, "the Flats."

Nearly one-fourth of the more than \$3 billion being invested in current and planned development downtown is slated for Public Square, site of the historic Tower City shopping and office center. The Warehouse District draws crowds and residents with restaurants, upscale apartments and boutiques. Playhouse Square showcases national acts in four elegantly restored theaters from the 1920's and 30s that comprise the third largest performing arts center in America.

As the nation prepares for the challenges of the 21st century, Northeast Ohio has emerged as a shining example of a post-industrial region that has blasted off the rust, yet retained its hearty character. Indeed, this thriving community has fought hard for more than two decades to rebuild its physical and economic core and revive its proud image, accumulating accolades along the way faster than you can say "Comeback City":

Achieved unprecedented rank as five-time winner of the National



*Jacobs Field and Gund Arena, completed in 1994, draw sell-out crowds to the \$435 million sports and entertainment complex and surrounding businesses. Photography provided by Mort Tucker*

Civic League's prestigious *All-America City Award*

- Named one of the USA's TOP 10 Cities for U.S.-based Global Companies by *World Trade Magazine*
- Cited by President Clinton as "a model for economic growth throughout the country"
- Listed as one of the best cities in which to start and own a small business by *INC. magazine*, with 6,000 business startups occurring each year
- Ranked in the top 5 percent of North America's metropolitan areas by *Places Rated Almanac*

The most exciting news is that—whether related to the blues, baseball or business—the intangible enthusiasm coursing throughout the region is here to stay. You see, it is all founded on a rock-solid base of revitalized manufacturing, an improved economic situation, a growing service sector and a rapidly expanding reputation as a fun-filled vacation destination.

Consider these facts: Northeast Ohio accounts for approximately 40 percent of Ohio's business activity. Greater Cleveland currently possesses the 9th

largest industrial market in the U.S. with more than 6,000 manufacturing concerns representing roughly 75 percent of all Standard Industrial Classification. According to a 1994 study by *Site Selection* magazine, the Cleveland area ranked third among the nation's 327 metropolitan areas in new facility and business expansion.

Moreover, service jobs now comprise 32 percent of Greater Cleveland's employment, while manufacturing jobs claim 18 percent. This diversification of its economic base has created a whole new array of trade and investment options for the



*The \$92 million Rock and Roll Hall of Fame and Museum, located at North Coast Harbor on Lake Erie, opened in September 1995. Photography provided by Mort Tucker*



Additionally, the city has a skilled workforce in excess of 900,000, and it is ranked as the 13th largest consumer market in America with 44 percent of all households in a 500-mile radius. Cleveland has become an increasingly attractive place for business expansion and relocation, and we're well positioned to compete in the global marketing environment of the 1990s," says Mayor George V. Voinovich. "One reason for this success has been the spirit of cooperation between our public and private sectors. People here joined together, setting personal agendas to build a new city as a great place to visit, a great place to do business and a great place to live," says Governor George V. Voinovich.

## NORTHEAST OHIO REGION STIRS UP ECONOMY

Internationally acclaimed as The New American City, Cleveland has primed the Northeast Ohio region for a new economic revolution. To Cleveland and Geauga County's west, Lorain County is dedicated to heavy industry, and strives to reinvent itself through creating new kinds of technologies, products and businesses as well as improving its infrastructure and explorative partnerships.

"We were using the team concept in business before teams became fashionable," says George Manos, assistant to the president, USS/KOBE Steel. "We've got people from the Lorain County Department of Commerce to business to come on getting together to rebuild our community and position ourselves for the 21st century."

To the east, Lake County may be the smallest county, but it has a vital economic presence, a commitment to high technology and business, and a definite world view. The leading export counties in the region make presently ships everything from chemical additives and automotive components to pressure-sensitive materials, fire prevention systems and small boats around the world.

"Lake County has large and small businesses, which represent both manufacturing and service concerns," says Michael Zarlenga, vice president of Zarlenga Industries, Inc. "We have such a diverse mix of industry that companies and workers alike can't help but find something to fit their needs."

Another of Cleveland's eastern neigh-

bors, Geauga County, blends centuries-old agriculture with 21st century manufacturing operations, producing everything from kitchen cabinets and Amish cheese to molds for polymer products. Richard Coyne, general manager of Jaco and Martone, an area business, says, "What we like best about the county is the feeling that we have room to expand, and we have. Our business is growing, and we couldn't have done that at our former location."

Known as the "Polymer Valley" because it is the world's leading polymer research and manufacturing center, Northeast Ohio is home to more than 1,200 companies engaged in the manufacture of coatings, plastics, resins, molds or extrusions. The North Coast region also numbers advanced machinery and equipment, biotechnology and medical products, headquarter/administrative office operations, aerospace industries and real estate/development investment amongst its key markets. Some 300+ industrial research laboratories combine with NASA Lewis Research Center and 22 area universities and colleges to make Northeast Ohio one of the top R&D centers in the world.

## TOURISM ATTRACTS PEOPLE FROM AROUND THE WORLD

If seeing is believing, people from all over the globe are opening their eyes to this remarkable rebirth. In fact, visitor inquiries are up 114 percent over 1994. Business leaders across the country recognize the area's tremendous achievements and powerful growth potential. Of course, in addition to an explosive economy, there's plenty of fun to be had in this fast-growing tourist mecca.

With the opening of the Rock and Roll Hall of Fame and Museum in Cleveland and Invention Place (Inventors Hall of Fame) in Akron to complement

the venerable NFL Football Hall of Fame in Canton, the region has earned the moniker, "the national hall of fame corridor." Next year, the \$55 million Great Lakes Science Center, featuring exhibits on science, the environment and technology, will open beside the Rock Hall. And all the amusements of Cedar Point, Sea World and Geauga Lake are within an hour and a half of downtown Cleveland.

Just east of downtown, University Circle encompasses the nation's largest concentration of museums and cultural, educational and religious institutions, including the magnificent Cleveland Museum of Art and Severance Hall, home of the world-renowned Cleveland Orchestra. Nearby, the Cleveland Play House is the oldest operating regional theater in the U.S., and Karamu House is the nation's oldest African-American cultural institution. You can even find Cleveland on the World Wide Web by contacting <http://www.cleveland.oh.us>.

To foster further growth of business and tourism, Cleveland is committed to increasing air traffic through Hopkins International Airport, which already serves as a major hub for Continental Airlines and, along with two other commercial airports in the region, offers an average of 370 daily direct and connecting flights to domestic and international destinations.

Cleveland will have an ideal opportunity next year to show off the rich heritage and remarkable recent accomplishments of the region when it celebrates its Bicentennial. In 1896, when the city recorded its 100th birthday, Cleveland was acknowledged as an industrial giant.

Now, the Bicentennial will highlight the dramatic success story that reveals Cleveland and the North Coast Region as a progressive, post-industrial powerhouse—a New American City ready to lead the world into the next century.



An ore boat unloads cargo on the Cuyahoga River at Cleveland Works - LTV Steel. Photography provided by Dave Rentsch



# Ohio's Jobs Bills: A Formula For Prosperity

When Consolidated Stores Corporation decided to expand its Columbus-based distribution center, the company became a test case for the government-business partnership touted by Ohio's government leaders. The question was: how can the state help us expand our business and create new jobs? The answer came in the form of a 70% tax credit over ten years to help the company finance its \$25.8 million project. Consolidated's contribution to the partnership: 200 new

jobs created and 1,545 jobs retained.

Consolidated is just one of 294 Ohio companies that have expanded or relocated in the state since February 1993, in large part because of the financial incentives offered under Ohio's "Jobs Bills." That adds up to a \$3.6 billion investment in the state and the creation of 34,020 new jobs and 44,594 retained jobs.

The first two versions of the Jobs Bills provided for a wide variety of tax incentives, ranging from research and development measures to export tax credits. The strategic base of the bills, however, lay in the Job Creation Tax Credits included in them. The tax credits provided for an attractive government-

business trade-off: if business will commit to creating more jobs, government will commit to tax incentives that are a true financial asset for a company.

The latest version of Ohio's business enhancement initiative, Jobs Bill III, attempts to build upon the momentum created by the first two bills by revamping huge portions of the state tax code to create a more business-friendly environment, while helping communities and distressed regions. At the same time, the measure puts some muscle behind efforts to remove the bureaucratic obstacles that have hindered business growth in the past.

## OHIO'S JOBS BILLS AT A GLANCE

### Just A Few Highlights Of Ohio's Jobs Creation Measures

|                                     |                                                                                                                                                                                                                                                             |
|-------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Job Creation Tax Credit             | Encourages investment and job creation by giving a tax credit based on the state income tax paid by full-time employees. The amount of the tax credit can be up to 100% for ten years. So far, the Job Creation Tax Credits issued have ranged from 40-80%. |
| Export Tax Credit                   | Rewards companies that expand export activity by granting them eligibility to claim up to a 10% credit on pre-tax profit from the expanded export operation.                                                                                                |
| Research And Development Tax Credit | Companies that purchase equipment for research and development activities are exempt from state and county sales taxes normally paid. Exemption covers equipment used in either directed or pure research.                                                  |
| Investment Tax Credit               | Gives tax credits for 7 1/2%-13 1/2% of a company's investment in productivity enhancing machines and equipment.                                                                                                                                            |

*The winning  
Strategy*



four of America's Sea World Marine Life Parks, like this one in Aurora, Ohio, use vane-type actuators especially designed by Parker to control underwater gates that enable the killer whales and dolphins to enter and exit their pools. Shown are Bruce Kohlmeyer, the Manufacturing Manager of Parker's Wadsworth, Ohio Division where the actuator was designed and developed - and his family - with Shamu<sup>®</sup> the killer whale.



Photo courtesy Sea World of Ohio.

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Parker was founded in the Greater Cleveland area in 1918 and has been headquartered here ever since.

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# Export Growth

Even before the latest Jobs legislation passed, the effort at a more realistic and efficient government-business relationship was reaping benefits.

A prime example is the advances Ohio manufacturers enjoyed in export trade, a key target of the initial Jobs Bill. More American manufacturers are now exporting from Ohio than any other state. In 1994, 1,732 of the state's 2,575 manufacturers (67%) were engaging in some form of export, an impressive figure that *World Trade* magazine said "validates Ohio's standing as a world-class state." Other analysts have described Ohio as "visionary" in creating an "export-friendly" state. The state is the only one in the U.S. to offer the innovative incentive of the Export Tax Credit, which has had the effect of demonstrating both the ease and the advantage of exporting. Whatever description is used, the bottom line of the story is simply that Ohio manufacturers are selling more of their products because they're now selling to the world.

*The winning strategy*



| State/Rank      | Total Exporters | Total Manufacturers | % Manufacturers That Export |
|-----------------|-----------------|---------------------|-----------------------------|
| <b>1. OHIO</b>  | <b>1,732</b>    | <b>2,575</b>        | <b>67%</b>                  |
| 2. California   | 1,609           | 2,709               | 59%                         |
| 3. Illinois     | 1,602           | 2,500               | 62%                         |
| 4. Pennsylvania | 1,393           | 2,344               | 59%                         |
| 5. Michigan     | 1,250           | 1,837               | 68%                         |
| 6. Indiana      | 976             | 1,562               | 62%                         |
| 7. Texas        | 866             | 2,177               | 40%                         |
| 8. New York     | 766             | 1,889               | 41%                         |
| 9. Wisconsin    | 719             | 1,105               | 65%                         |
| 10. Georgia     | 674             | 1,349               | 48%                         |

Source: *World Trade Magazine*

## Reforms At Home

The Voinovich administration's pledge to clean up Workers Compensation regulations, a long-time business community irritant, led to a series of sweeping reforms. The result was a 7.3% drop in average workers comp premium levels as of July 1, a reduction of \$120 million in the premiums paid by Ohio's employers. Under the reforms, the Bureau of Workers Compensation itself was able to wipe out a 14-year deficit, and as of September 1, the Bureau reports directly to Governor Voinovich, so reform can be institutionalized.

"The reforms in Workers Compensation are a good example of how the state of Ohio is doing more than just paying lip service to working with business," says Roger Geiger of the National Federation of Independent Businesses. "The state has a commitment to being a more 'user friendly' place to do business."

Communicating that commitment is the responsibility of the state's Department Of Development, headed up

by Don Jakeway. "We're here to tell business people what Ohio has to offer them, find out what else they need, and then do our best to go get it for them," Jakeway says.

The national and world community appears to be recognizing the success of the Department's efforts. The American Economic Development Council recently honored the Department's work with awards for marketing the state's business climate. And the Department was the only state agency to make *Selection* magazine's top ten list of outstanding development groups around the world.

"The state's Department Of Development gives business a true partner in pursuing growth and success," says John Pepper, Chief Executive Officer of Procter & Gamble. "The people who staff the Department are united in an understanding of all our commitment to the needs of business and in implementing a strategy that is good for business. They're allies rather than adversaries."



# HOT SPOT

For Business Development.

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Marathon Oil Company, Cooper Tire & Rubber Company, OHM Corporation, Whirlpool Corporation, Harris Corporation, Dow Chemical, and many other major corporations have found Findlay, Ohio to be the perfect place to conduct world-wide business, and... **Relax, Raise a Family, and Enjoy Life.**

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See for yourself why Findlay is **Ohio's HOT-SPOT for Business Development.** Contact Foundation President, John L. Kovach for a confidential discussion of the opportunities available.

Access information about Findlay through **Ohio ON-LINE.**





# Ohio's Global Growth

If Ohio were a country, it would rank as the world's 16th largest economy, illustrating its standing in the global marketplace. But a true indicator of the state's move into the worldwide business atmosphere is revealed in the recent figures on the number of Ohio companies that actually deal in the global market.

Ohio has become the number one export state in the U.S., based on the number of manufacturers who export their goods. More than two-thirds of all Ohio companies with more than 100 employees now sell their products abroad. It means that a state with a population of 11 million people has become the nation's leader in moving U.S.-made goods into foreign markets.

Success in that arena can significantly raise the stakes for American companies and their employees. A recent report by the National Association of Manufacturers showed that workers at exporting companies earn an average of 15% more in pay and 33% more in benefits than their counterparts at non-exporting companies. The report also revealed that employees of exporting companies are 30 to 50% more productive, better skilled and trained, and have greater job stability. In essence, companies realize a

greater value in the employee base when the workers themselves are "world-class."

And exports are clearly trending upward. The same report showed that during the past ten years, exports have accounted for about one-third of all economic growth in the U.S.

The growth of export business in the Buckeye State has been, in large part, a result of Ohio's incentive programs. The Jobs Bills contained major measures that provided refunds on state corporate and franchise taxes when companies increased export sales. That, coupled with an aggressive effort to recruit more exporters, and innovative programs to simplify the export process, have given large and small companies alike access to valuable new markets previously ignored.

"We've aggressively pursued companies that haven't exported in the past," says the Department of Development's Don Jakeway. "We're able to show them how the state can make exporting both easier and more profitable."

One way of making the process simpler lies in the information technology Ohio offers its companies. The Ohio On-Line Export Directory is an interactive, computer-based catalogue that displays products and services needed in world markets, as well as information on state programs available to get export trade moving.

While the economic incentives for export have proved highly attractive to Ohio companies, the state's targeted-industry approach to help grow world markets goes back several years. Honda originally planned only a motorcycle plant when it decided to open U.S. operations back in the 1970's. But after seeing the state's Transportation Research Center, a facility for the testing and development of transportation products, Honda officials decided to add some wheels. Today, Honda employs 10,000 workers in the state at an engine plant and two auto production facilities.

"Ohio showed us that it was willing to put some meaningful support behind its business efforts," says Susan Insley, Senior Vice President, Honda Of America Manufacturing.

That feeling may be the reason Ohio ranks sixth in the nation in Fortune 500 companies that have their corporate

headquarters in the state. Names like Rubbermaid (*Fortune's* Most Admired Company two years in a row), Goodyear, Procter & Gamble, Parker Hannifin, Timken, TRW, Worthington Industries, Dana Corporation, and The Limited all make their corporate homes in Ohio. Other major companies, like ABB, Ford, G.M. and G.E. maintain a huge presence in the state. Recent major expansions in Ohio by companies like Cooper Tire and Spiegel were the result, say market experts, of an understanding that Ohio was serious about giving business the tools to prosper.

## NAMES WITH A MAJOR PRESENCE ON OHIO'S BUSINESS SCENE

**Huntington Bancshares Inc.**

**American Electric Power**

**Worthington Industries**

**The Scotts Company**

**Consolidated Stores     The Limited**

**American Greetings     Cooper Tire**

**Cincinnati Milacron     Banc One**

**Procter & Gamble     Goodyear**

**Bob Evans Farms     Chrysler**

**General Electric     Borden**

**General Motors     Honda**

**Compuserve     Dana**

**Rubbermaid     Ford**

"The state's leaders have shown a willingness and the courage to create wealth for the citizens of the state by making an investment in a better business climate," says Frank Wobschlag, Chairman and Chief Executive Officer of Huntington Bancshares Inc.

It is not just the big names taking advantage of that better business climate. Companies like Bry-Air, though not yet be worldwide names, have seen impressive growth in the past several years, largely because of the incentives and support the state provides.

"For a smaller company like ours, Ohio offers a tremendous advantage," says Bry-Air's Paul Griesse. "We've been able to use the resources the state has to grow both locally and in the world marketplace."

*Good company  
in the  
nation state*





## Your Business Is Growing. Congratulations. Who's Going To Do All The Work?

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You see, at MRI, we're here to help you grow. Especially when you're growing.

Sales Consultants

Management  
Recruiters

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**MRI** Intelligent Staffing Solutions.™





**John D. Ong**  
(Chairman & CEO)

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BFGoodrich is a company with a proud heritage. For 125 years the company has built its reputation on quality products, customer service and technical excellence.

The company's legacy extends to Dr. Benjamin Franklin Goodrich, who established the first rubber company west of the Allegheny Mountains in Akron in 1870. Since that time, BFGoodrich has expanded its manufacturing and marketing activities throughout Ohio and the world.

No longer a tire manufacturer, today BFGoodrich provides aircraft systems, components and services and manufactures specialty chemicals.

BFGoodrich has been building on its core of specialty aerospace businesses since the mid-1980s. BFGoodrich Aerospace provides landing systems, safety systems and aircraft sensors and related equipment to aircraft manufacturers and operators worldwide. BFGoodrich Aerospace also provides aircraft maintenance, repair and overhaul services through an expanding network of service centers.

BFGoodrich also has been expanding its specialty chemicals businesses. BFGoodrich Specialty Chemicals provides specialty plastics, specialty additives, sealants, coatings and adhesives. These products are used in a broad range of applications from telecommunications equipment and construction materials to pharmaceutical and personal care products.

For more information about The BFGoodrich Company, please call: (216) 374-3557.



You will discover Ohio's best opportunity and an excellent business climate in Guernsey County. Beyond our highway advantages, beyond the productive and available work force, beyond our lower costs and tax advantages, you will also find a superior quality of life. For additional information, please call Al Hills, Economic Development Director of the Cambridge-Guernsey County Community Improvement Corporation, at (614) 432-1881.

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*(gathering place, principal town)*

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Economic growth is our future!  
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a good place  
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Improvement  
Corporation**



**A Great  
Location  
For Your  
Company**

Find out why well-known companies have chosen this community with a reputation for friendliness, hospitality and great city pride.

Located on I-75, Troy is only 10 minutes away from the "Crossroads of America" intersection of I-75 and I-70, and 15 minutes away from the Dayton International Airport. Attractive tax incentives and excellent sites. For more information contact Roy E. Carlson, Troy Development Council, P.O. Box 218, Troy, OH 45373. Phone 513-339-7809. Fax 513-339-494.



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the rewarding promise of an outstanding college education.



We're one of the region's largest industrial employers. But our commitment can't  
be measured by numbers alone. We're at home here. Close to the heart of the city.

**And its people.**





# Ohio Puts Its Heavy Hitters To Work For Companies

In the pleasant small-town atmosphere of Fostoria, Ohio, Norton Manufacturing Company wasn't exactly considered a dominating presence on the national business scene. But the company, which produces precision crank shafts for the auto industry, recently took a premier position when it became the first company in the U.S. to implement new National Skill Standards among its employees. Skill standards are the benchmark levels of knowledge and competence required to perform work related functions in a given industry, part of a nationwide attempt to meet new industrial and technological demands with definable standards of knowledge and capability.

Norton's breakthrough achievement was made possible by a state grant of \$100,000 to retrain its workers to meet the new metalworking National Standards. As a result, the company figures to improve on world-class quality standards.

"We've seen first hand how the state's interest in business and the resources it

provides can translate into a successful effort," says Norton's Chief Executive Officer Richard W. Norton.

Because of the value-added philosophy that gave birth to the state's Jobs Bills, the administration has developed a team approach to business assistance that's directed at getting meaningful results for Ohio companies. The governor's inter-agency task force was developed to assist businesses in getting from concept to reality hassle-free as a one-stop information center that guides a business through the entire location or expansion process.

In much the same way, the administration's network of regional representatives acts as a liaison between the state government and business and civic organizations to get expansion or relocation projects going in specific regions of the state. The state's 12 regional economic development offices provide communities and companies local access to all state development programs, while permitting the Department of Development to respond to fast-breaking events and opportunities at the local level.

"Our regional rep helped us get our projects off the drawing board and to the groundbreaking stage," says Maynard Sauder of Archbold, Ohio's Sauder Woodworking, whose company will add 1,200 jobs as the result of a \$50 million expansion project. "To me it's part of the added value of doing business in Ohio; you have an ally who can get the job done for you."

The Governor's Human Resources Investment Council is another team concept approach that is bearing fruit. The Council acts as a multi-jurisdictional clearing house to facilitate worker training and employee procurement, helping companies find the right workers with the right training.

But all those programs and organizations won't help much unless Ohio's communities can get out and sell their product, economic opportunity, to the business world. Ohio has launched a series of innovative programs and impressive partnerships aimed at educating business leaders about

finding the right match for their companies in the Buckeye State.

Nowhere is that effort more apparent than in a breakthrough initiative dubbed "First Frontier." Originally conceived to help the state's once-economically disadvantaged Appalachian counties, First Frontier has expanded to small communities and counties throughout the state. The program puts economic and strategic vision behind a plan to attract business to those areas, by matching their varied resources with companies that have specific needs. The state uses its resources to help local communities construct and implement their own national marketing and advertising programs, an example of teamwork approach Governor Voinovich promised in vowing to give local communities a voice in their own development efforts.

"With all of these programs, Ohio is demonstrating that it can create a user-friendly, value-added environment that really works for business," says John Miller of Superb Manufacturing, one of the emerging leaders in exports. "The state has a truly unique system, because it constantly re-examines its efforts to keep pace with the changing realities of the business world. Ohio's being extremely innovative."

For Governor Voinovich, accolades like that are welcome, but the real proof of the effectiveness of the teamwork approach lies in the facts.

"When you see a giant company like Ford invest a billion dollars in Ohio when you see big names like Procter & Gamble invest \$280 million in a research and development facility, when you see other big names like G.M., The Limited, Panasonic, USS/Kobe, Meijer, Kohl's, Honda, and Chrysler with major expansion efforts, and you combine those with the progress shown by dozens of companies like Norton Manufacturing, I think that says something about how this state is working for and with business," Voinovich says. "It shows we have the commitment and the desire to make the best possible environment for all size business."

*A team effort  
to get down to  
business*



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that takes three years to get to market?**

Mike Hogue  
Chairman  
Hogue Cellars



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## Shrinking The World Marketplace

The cost of getting to market is a major competitive issue in any business. Ohio companies get a head start on success thanks to both Ohio's unique location, that puts them close to their markets, and a far-sighted plan to improve transportation systems to meet the global business demands of the new century.

Its geographic setting makes Ohio the transportation crossroads of the nation. That fact, and the effective business-government partnerships established in the state, mean Ohio has become a favored location for national distribution centers. Companies like Kohl's, Spiegel and Meijer have all recently joined the growing list of firms that center their distribution operations in Ohio.

The state is located within 500 miles of three-quarters of the U.S. population and 70% of the nation's manufacturing facilities. It has the country's fourth largest interstate highway system and ranks third in the U.S. in paved

highway mileage. It's central location is one reason Ohio is home to the nation's major regional and national trucking lines, and a favored home for LTL (Less than Truck Load) carriers.

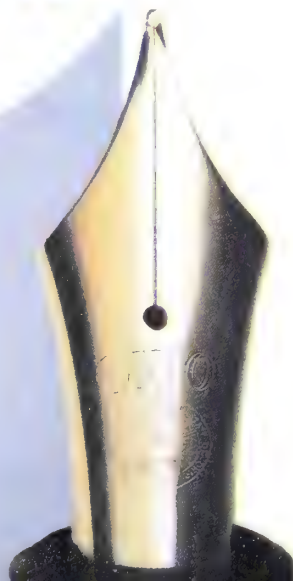
The state's 184 public airports, handling some 13.4 million air passengers, put Ohio businesses within an hour's air travel of two-thirds of the American population. Air Cargo facilities dot virtually the entire state map, with companies like Airborne Express operating out of Wilmington, Emery Air Freight in Dayton, and Burlington in Toledo. The Rickenbacker air facility near Columbus is an air cargo industrial park with foreign trade zone status.

Access to water routes offer another decided advantage. Each year some 120 million tons of cargo are shipped through port facilities on the state's 265 miles of Lake Erie shoreline and the 450 mile stretch of the Ohio River, making Ohio one of the national leaders in cargo shipping.

Ohio's rail cargo facilities also bring markets closer to home. The state has 6,458 miles of rail track, and boasts eight foreign trade zones with rail service.

Now the Voinovich administration has embarked on a series of initiatives aimed at capitalizing on and expanding the added value Ohio brings to business transportation needs. An ambitious program called "Access Ohio" has become a formal ratification of the fact that state leaders won't rest on the laurels of the state's geographic advantages in providing a competitive edge. Access Ohio is a comprehensive plan for assessing and upgrading all facets of the state's transportation systems, coordinating them under a singular mission to develop an even more efficient intermodal network.

*Market  
access*



## STAR BANK One Of Ohio's Surest Signs Of Growth

Since 1863, Star Bank has been growing with the businesses and the communities of the Ohio-Indiana-Kentucky tri-state region. As the major subsidiary of the \$9.2 billion Star Banc Corporation holding company, Star Bank has the financial resources to meet the credit needs of businesses large or small and the expertise to structure financing to fit your situation.

Star is one of the outstanding banks in the region, providing traditional corporate lending, as well as structured capital, equipment finance and leasing and commercial real estate. Recognizing that loans are only part of a good banking relationship, Star augments lending services with a full line up of non-credit support services, including comprehensive cash management capabilities, employee group banking packages and investment options.

Star Bank's international trade services division has been the recipient of awards from the U.S. Department of Commerce and the State of Ohio.

Star Bank's Small Business Banking division specializes in meeting the unique needs of businesses with annual sales up to \$3 million. Star's market knowledge, total relationship management and expertise can increase borrowing potential and simplify procedures, making Star a valuable business partner.

Star Bank offers a full range of corporate trust services, including structured finance and custody, bond servicing, stock transfer and employee benefits planning.

With more than 250 full-service banking locations and more than 350 ATMs, you're never far from Star Bank, wherever you live or locate your business.

g statistically valid, regionally  
ed criteria, state officials have  
ed critical intermodal corridors  
ove people and products to the  
the nation and the world. The  
ermits the state to set priorities  
grading and integrating these  
routes into a seamless network  
transportation modes. Perhaps more  
antly, the Access Ohio plan sets  
strategic map of funding  
es, identifying stable revenues  
preservation and maintenance  
ing facilities and the  
uction of new transportation  
ces.  
ess Ohio isn't just a technical  
intended to produce a list of  
y construction projects," says  
or Voinovich. "This program is  
conceived, strategic approach,  
sound funding platform, that  
e Ohio tremendous advantages  
s transportation resources."

## Major Goals Of Access Ohio

- **Preservation And Management**—Preserve and manage Ohio's existing multi-modal transportation system and resources more effectively and efficiently.
- **Economic Development And Quality Of Life**—Enhance Ohio's comparative economic advantage and quality of life, and expand the diversity of the state's economy through safe, convenient and efficient transportation systems.
- **Cooperative Planning And Efficiency**—Utilize cooperative planning processes through system management programs and public participation.
- **Transportation Safety And Convenience**—Improve the safety of transportation systems while maximizing the value of the state's transportation investment.
- **Funding**—Seek stable revenues for the preservation and maintenance of existing facilities and services as well as new ones, while developing innovative approaches to transportation funding.



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Since 1895, we've taken great pride in calling Ohio "The Land of Lincoln." Throughout the years, we've been a world leader in arc welding products, cutting equipment and electric motors.

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And our commitment to education in Ohio has never been stronger. We've recently established Lincoln Electric's "Welding and Cutting Education 2000," an accredited seminar that's available to high school and vocational teachers throughout Ohio. We've also opened the doors of our Welding Technology and Training Center to thousands of individuals from around the world.

It's been an exciting century of growth, discovery, and progress, and on this, the celebration of our 100th Anniversary, we would like to extend a heartfelt thanks to our state — a very special place that we are honored to call "home."



Donald F. Hastings  
*Chairman  
Chief Executive Officer*





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## A Leader Among World Economies

Ohio's economy, judged by gross state product, is the seventh largest in the nation.

As a nation within a nation, Ohio's economic strength springs from a richly

*Ohio is a nation  
within a  
nation*

diverse and uniquely varied patchwork of social and geographic characteristics. Unlike almost any other state, Ohio is virtually impossible to typify. *World Trade* magazine was speaking of Ohio's export leadership when it described the state's standing as "world class." But export strength and development leadership are only parts of the story in Ohio's emergence as a true nation-state, an independent and self-reliant player on the world scene.

To begin with, no one or two major cities dominate Ohio. Ohio is home to eight urban centers (as classified by the U.S. Census) and 15 "micropolitan" communities, the mid-sized towns that blend the best of big city and small town life.

From the large to the small, Ohio's communities have garnered a major share of the recognition national analysts bestow upon those that are the "first" or the "best." The "Places Rated Almanac" rated Cincinnati #1 as a place to live,

(continued on following page)



**Robert W. Gillespie**  
Chief Executive Officer, KeyCorp

Eighteen months ago, Bob Gillespie was a central player in one of the country's largest bank mergers, a union that created the tenth largest U.S. bank holding company. As he takes the CEO reins of Cleveland-based KeyCorp on Sept. 1, he oversees a franchise of 1,400 branches and offices that stretches from Maine to Alaska, and is often called the broadest distribution network of any bank in the country. With about \$68 billion in assets, KeyCorp today ranks as one of the largest financial companies in the U.S. in terms of small business financing, corporate banking, trust and investment management and consumer lending.

At 51, Gillespie is one of the younger members of the elite group of CEOs who run the country's biggest financial services companies. He began with a much smaller and much smaller Society National Bank in Cleveland in the late 1960s on a part-time basis while completing graduate work in business administration at Northeast Case Western Reserve University. He is a graduate of the Harvard University Graduate School of Business Advanced Management Program.

"Ohio is a natural location for the headquarters of the new KeyCorp," says Gillespie, "given its central location for a nationwide company, transportation and momentum that Cleveland, and indeed, the State of Ohio continues to establish as a world-class center for commerce, travel and entertainment."





**Tibor Kalnoki-Kis**  
President and General Manager  
Electronic Power Sources,  
Gould Electronics, Inc.

## TECHNOLOGICAL BREAKTHROUGHS DO OCCUR OUTSIDE OF THE SILICON VALLEY.

Electronic Power Sources (EPS) Division of Gould Electronics Inc. has introduced the POWERDEX® brand of innovative primary and rechargeable lithium batteries. Led by Dr. Tibor Kalnoki-Kis, this Northeast Ohio company is on a mission to "redefine the battery market landscape." The new technology serves diverse market segments as: super computers, computers, telecommunications, security control, etc.

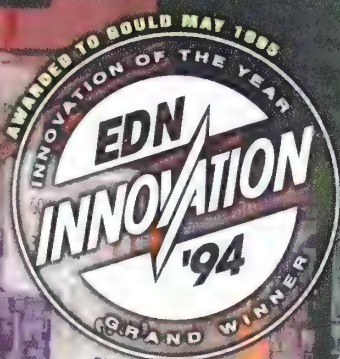
May, the POWERDEX® 3C050M has earned the prestigious "Innovation of the Year Grand Winner" award in the Power Sources Category from *Electronic Design* magazine. At less than 0.7 mm in thickness, it is the world's thinnest lithium battery produced in OEM quantities.

POWERDEX® batteries are gaining acceptance around the world because they combine the advantages of the lithium battery system, their high energy density and long shelf life, with the wafer-thin format. "Our battery technology allows customers to differentiate their product, reducing manufacturing costs," says Dr. Kalnoki-Kis. "As a result, new applications are evolving constantly."

The company is expanding its facilities in Eastlake, Ohio, in response to the growing worldwide interest. "Gould is, and will continue to be, the worldwide leader in introducing this technology in OEM quantities," says Dr. Kalnoki-Kis.

ultra thin, ultra light, high energy  
lithium batteries

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35129 Curtis Blvd., Eastlake, OH 44095-4001, USA

(continued from previous page)

while "micropolitan" Lima has won honors as the best value in the U.S. the most inexpensive place to live and work) and Cleveland, meanwhile, notched its record 5th "All-American" city award.

When the Almanac Of American Politics refers to Ohio as "arguably the pivotal state in national politics", it is referring to the quintessential American state, a place where east meets Midwest, and north meets south. The state just may be first in

the "first" category. From the nation's first kindergarten to the first ATM machine, the fabric of Ohio life is woven in business, social and technological history. Hence the Inventors' Hall of Fame, the National Aviation Hall Of Fame, as well as the Pro Football Hall Of Fame and the Rock and Roll Hall Of Fame all call Ohio home, as do the world's largest advertiser, Procter & Gamble and America's most admired corporation, Rubbermaid.



## Ohio's Advanced Education System

More than 100 colleges and universities

38 separately governed, state-assisted colleges and universities

13 state universities

2 free-standing medical schools

24 state university regional campuses

15 community colleges

8 technical colleges

More than 70 independent colleges and universities

The strength and diversity of Ohio's educational system not only contribute to a wealth of educational opportunities, but provide a wellspring of highly trained talent for business. Education, meaningful, life-long learning, is no more than 30 minutes away from any Ohio



resident anywhere in the state.

More than 533,000 students attend advanced education classes in Ohio, with more than 50,000 of those at The Ohio State University, the nation's single largest campus. Employers have often cited the ready availability of skilled, educated workers as a major reason for locating in Ohio.

Ohio's value-added, team approach to creating a partnership with business has led to a unique and on-going technical assistance program that pumps \$2 billion into the effort to help companies become more productive and competitive. Under Ohio's Thomas Edison Program, eight

technology research centers, covering a wide range of subjects from plastics to polymers to welding and advanced manufacturing, become a valuable resource for a company's research and development efforts.

But what many employers cite more than the

state as a reason for selecting Ohio, is the more subjective category of lifestyle. Surveys of

many business leaders indicate that workers have come to appreciate the added value of jobs in a state where costs are relatively low, opportunity is high, and where there is a social life to fit any preference.

"It may sound like a cliché, but Ohio truly is a state that offers something for everyone," says Ted Host, Chairman and Chief Executive Officer of The Scotts Company. "The diversity and availability of recreational and educational resources is something most smart business people look at when they think of locating here because it provides an added benefit and a better chance at business success."

*Ohio's  
advanced  
educational  
system*





# Marion means business!



**D**o you know where the world's largest manufacturer of clothes dryers is located? Where millions of responses to the Readers Digest sweepstakes are processed? Where the lion's share of popcorn is produced and packaged?

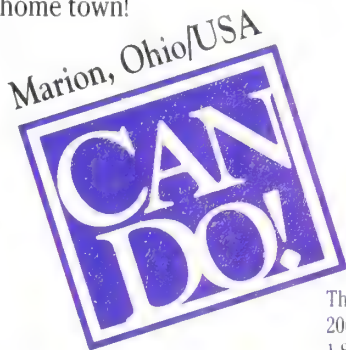
Where some of the most powerful accounting software in the world is created? Where to find the Memorial of the United States 29th President, Warren G. Harding? Marion, Ohio...the heart of Ohio, the heart of MidWestern America.

Whirlpool Corporation, Kable Fulfillment Services, Wyandot, Inc., and Macola Software all call Marion their home. And, this powerful micropolitan community is ready to meet your business

and industrial needs with more than a dozen prime development sites ranging in size from 5 to 1,500 acres. Positioned 40 miles north of the state capital, Columbus, Marion is central to 60 percent of the major North American trade markets.

Economic development is taken seriously here. The Greater Marion Community Area New Development Organization, Incorporated—more commonly known as CAN DO!—is poised and ready to assist with site selection, tax incentive programs, and a broad range of economic development services to meet the unique requirements of your company.

Information on the Marion area is available by contacting CAN DO! at the toll-free number or address below, or by browsing our pages in the Ads & Offers section of BusinessWeek On-Line via America On-Line. There you will find details on the labor market in Marion, area transportation capabilities, utilities, available sites, and quality of life issues. You can also get to know your potential neighbors by reading the features on some of Marion's major businesses and industries. Marion, Ohio...A good place for a home office, a great place for a home town!



1-800-848-1300



photos by Lausé Studios

The Greater Marion Community Area New Development Organization, Incorporated  
206 South Prospect Street, Marion, Ohio 43302  
1-800-841-7302 • Fax: 614/387-5522 • e-mail: Mrcando@aol.com



## Ohio's Development Team Is Dealing

Ohio's Department of Development Director Don Jakeway believes that, from the beginning, he enters into a partnership with a company, assuring business leaders that he and his entire team are working with the company's best interests in mind.

"What we've been able to do so far is convince business leaders that by doing business in Ohio, they can get the strategic edge they need to be successful," Jakeway says. "We've shown that there's a different attitude toward business in Ohio, and it's an attitude that can mean a lot for a company's bottom line."

Jakeway's staff has also made the entire process of relocation or expansion, from initial inquiry to final paperwork, a simplified and smooth procedure that's not unlike a customer's call to any private business.

"We're here to help you do business in Ohio," Jakeway says. "The move to a better bottom line starts with a simple phone call, a fax, or a letter to us. We'll take it from there."

To learn how you can sign on with Team Ohio's business success effort, if you want to find out more about the opportunities that await your business in Ohio, or if you simply have a question about how Ohio can help you toward a better bottom line, call or write:

Ohio Department Of  
Development  
Donald E. Jakeway  
Director  
77 S. High Street  
Columbus, Ohio 43266-0101  
1-800-345-OHIO  
FAX: 614-644-0745

## RPM, INC.

RPM, Inc., is a billion dollar specialty coatings company that has enjoyed 48 consecutive years of record sales, record net income and record earnings per share.

The company's more than 100 leading brand names typically command top positions in niches of huge industrial and consumer markets. RPM's major consumer brands include Rust-Oleum, Bondex, Zimsser, Testors, Bondo and Wolman, while its strong industrial brands include Day-Glo, Carboline, Mathys, Mohawk, Alumanation, Plasite and Stonhard.

Headquartered in Medina, Ohio, RPM operating companies in the state include Day-Glo Color Corp.; Republic Powdered Metals, Mameco International and Consolidated Coatings, all industrial and commercial waterproofing businesses; and Talsol Corporation, producer of Bondo auto body repair products and Mar-Hyde auto finishes for both the do-it-yourself and professional aftermarket.

Traded on the NASDAQ Stock Market under the symbol RPOW, RPM stock has provided investors with an average annual compounded total return (cash dividends reinvested plus market appreciation) of 23 percent a year since 1974.

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2628 Pearls Rd., P. O. Box 777  
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Some of RPM's leading consumer do-it-yourself brands.



**Duane E. Collins**

*President and Chief Executive Officer  
Parker Hannifin Corporation*

## PARKER HANNIFIN CORPORATION

We at Parker Hannifin are pleased to have our headquarters and 21 of the 151 manufacturing plants in our worldwide corporation based in **Ohio, the heart of it all**.

The strong Midwest work ethic Arthur Parker, an entrepreneurial engineer, led him to found his company here in 1918. That work ethic prevails throughout our organization today—in the form of premier customer service—from operations in Ohio and across the U.S. and Canada to Europe, Latin America and the Pacific Rim. Whether the customer needs precision actuators to control the pool gates for Shamu and friends, flight-control systems for jetliners, components for air conditioning and refrigeration systems, or seal devices to protect cellular phones from electromagnetic interference, Parker quality can be relied upon anywhere in the world.

We have earned that reputation because of our commitment to Parker's first Ohio tradition: premier customer service.

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JAMES C. COOPER & KATHLEEN MADIGAN

## FOR 1996, THE INFLATION TIGER LOOKS LIKE A PUSSYCAT

### U.S. ECONOMY

Inflation this year has looked a lot like one of those inept market launches from the early 1960s. It tried to clear the pad, but it just didn't have the power. And for 1996, inflation won't even attempt another liftoff.

That much seems clear from the nation's business economists, who gathered in San Francisco on Sept. 10 for the annual meeting of the National Association of Business Economists, during which a panel of 49 forecasters offered the first comprehensive look at what to expect next year (table).

The NABE forecasters don't look for the economy to soar in the coming year, a key factor in keeping inflation down, but they don't expect it to crash and burn in recession, either. They see a modest growth rate close to the economy's long-term trend of about 2.7%, which is consistent with stable inflation.

### BUSINESS ECONOMISTS ZERO IN ON 1996

|                    | '94  | '95  | '96  |
|--------------------|------|------|------|
| REAL GDP GROWTH*   | 4.1% | 2.0% | 2.7% |
| INFLATION*         | 2.6  | 3.1  | 3.2  |
| EMPLOYMENT         | 6.1  | 5.7  | 5.9  |
| MONTHLY ASURY BILL | 4.3  | 5.5  | 5.4  |
| YEARLY ASURY BOND  | 7.4  | 7.0  | 6.8  |

\*Q4 CHANGE, REST ARE ANNUAL AVERAGES  
NATIONAL ASSN. OF BUSINESS ECONOMISTS

They expect only modest deficit reduction for fiscal 1996, totaling some \$13 billion, relative to what current policy would yield. And they believe that the Federal Reserve will be steady as she goes. As a result, they see short-term interest rates fairly stable at current levels, and their projection for long-term rates reflects that stability.

### ON THEIR INFLATION FORECAST

is where the business economists seem most confident. They expect the consumer price index to increase 3.2% next year, about the same as the 3% pace anticipated for all of 1995. Federal Reserve Bank of San Francisco President Robert T. Parry, a noted inflation hawk, sounded even more sanguine when he told the audience, "I expect inflation to dip below 3% in 1996."

Inflation optimists have every reason to feel upbeat. Most recently, the August producer price index for finished goods fell 0.1% from July, and excluding energy and food, the core index rose a mere 0.1%. After accelerating earlier in the year, PPI inflation has fal-

len back to 1.3%. That's lower than a year ago.

And if you were worried that accelerating prices for intermediate goods would work their way forward to finished products, you can rest easy. The earlier runup in intermediate goods inflation had little, if any, impact, and prices at earlier production stages are now slowing (chart). Prices of intermediate goods have not risen for two months, and prices of crude materials have declined in three of the past four months.

The glowing PPI report on Sept. 12 fueled strong rallies in both the stock and bond markets. The yield on the benchmark 30-year Treasury bond dipped to 6.5%, the lowest since early July, and the major stock indexes climbed to record highs. The excellent price performance holds open the chance for another interest-rate cut at the Fed's Sept. 26 policy meeting.

### AUGUST RETAIL PRICES

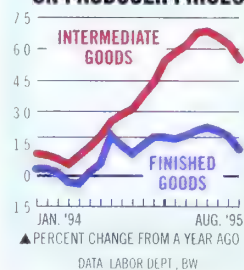
only reinforced the markets' optimism. The consumer price index rose only 0.1% in August, with the core index up only 0.2%. Prices of consumer goods were unchanged for the third month in a row, and service prices rose a slim 0.2% for the second consecutive month. Annual consumer inflation, running at 2.6% in August, seems likely to end the year very close to the NABE's 3.1% projection.

In fact, inflation is giving every signal that it has peaked for this phase of the business cycle, and that in 1996 it might well come in below its 1995 rate. The chief reason is the Federal Reserve's success at slowing the economy. That slowdown has resulted in an apparent peak in the rate at which the economy uses its production capacity and its labor.

As a result, the gap between actual and potential GDP, a measure of price pressures in the economy, reopened this year. Strong growth in 1994 had closed the gap, raising inflation concerns. This gap will appear even larger when the Commerce Dept. shifts to its new measure of gross domestic product in December, since the new numbers will show significantly less growth.

As the NABE points out, new fiscal restraint and a likely softness in oil prices are also inflation pluses. The current increase in worldwide demand for oil can be met by non-OPEC producers, so OPEC has no leeway to raise prices without losing market share. And def-

### WANING PRESSURE ON PRODUCER PRICES



DATA: LABOR DEPT., BW



## Business Outlook

icit reduction will take stimulus out of the economy:

And don't forget, the CPI itself is overstated: It omits how consumers substitute cheaper items over time. It overlooks new products. And it misses quality improvements. The NABE says when the government re-benchmarks the CPI in 1998, inflation will end up 0.5 to 1 percentage point lower than the current measure.

But probably the most compelling reason for expecting lower inflation in 1996 is the recent strong growth of productivity and what that means for unit labor costs. As it turns out, productivity, measured as output per hour worked in the nonfarm sector, increased at the sterling annual rate of 4.8% in the second quarter, the largest increase in nine years. The Labor Dept. revised last quarter's reading up sharply from the already healthy 3% advance first reported.

**AS A RESULT, UNIT LABOR COSTS** last quarter were no higher than they were a year ago. That's the first four-quarter period of zero growth in 30 years (chart). Unit labor costs are wages and benefits adjusted for productivity, and they act as a floor under inflation, because labor is two-thirds of a product's price. If they are slowing, inflation has room to slow, too.

Although the December GDP revisions will result in lower productivity growth than under current measures, unit labor costs may not be affected proportionately. Some analysts believe that compensation will be

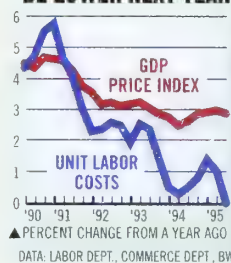
revised somewhat lower as well. So the performance of unit costs should remain excellent.

That showing sets this inflation cycle apart from others. By this time in past expansions—those that lasted 4½ years—the annual pace of unit labor costs had accelerated, as had inflation. By this time in the 1980 upturn, annual unit costs were growing 4.1%. The on-time unit labor costs rivaled their current performance was in the early '60s—when inflation was about 1%.

What could knock the 1996 inflation forecast askew? Keep an eye on service prices. Despite the stellar outlook for goods inflation, service prices are half of the CPI, and service inflation has risen to 3.4% in August, from 2.9% for all of 1994. Although there is plenty of anecdotal evidence to the contrary, measured productivity gains in services have not matched those in manufacturing, so unit labor costs are growing faster.

However, that could be just a measurement problem, since gauging the output of a bank or an accounting firm isn't easy. If so, just like one of those old Vanguard missiles, the recent pickup in service inflation is likely to fall back to earth as well.

### WHY INFLATION WILL BE LOWER NEXT YEAR



## BRITAIN

### AFTER A HIKE TOO FAR, AN INTEREST RATE CUT?

Just as in every meeting since February, the monetary powers in Britain left interest rates unchanged at their Sept. 7 meeting. Unlike the past four meetings, however, Bank of England Governor Eddie George likely did not ask Chancellor of the Exchequer Kenneth Clarke to raise rates.

George publicly backed away from his rate-hike campaign in a speech to mortgage lenders on Sept. 12. The shift reflects the economy's weaker

tone, which grew 2.8% in the year ended in the second quarter, down from a 3.7% pace in the first and 4.1% in the fourth. Any sector not benefiting from the export boom is in recession.

The third quarter is not starting off well, in part because almost all of last quarter's growth came in inventory accumulation. And businesses are now paring the excess stock levels. As a result, factory output in July unexpectedly tumbled 0.4%. Yearly production rose only 1.3% in July, the slowest pace in 1½ years (chart).

### A SHARP SLOWDOWN AT THE FACTORY



pushed the base lending rate to 6.75%. Housing starts plunged 21.1% in July from a year ago, and retail sales have fallen off. The Confederation of British Industry's survey showed that more

retailers reported declining sales in August than rising sales.

Employment is also suffering. After falling sharply in the previous two years, the jobless rate has hardly moved since April. August joblessness stood at 8.2%, and the annual pace of weekly earnings slowed to 3¼% in July, from 3½% in June, a sign of easing inflation pressures.

After their meeting, Clarke dismissed any notion of recession, but he was more upbeat about 1996 than most private economists. George likely remains concerned that inflation is still above the government's target of 2.5% for its preferred gauge: retail prices less mortgage interest. But amid signs of spreading weakness, the odds of a rate cut—perhaps before yearend—are rising.

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AUTOS

# LET'S MAKE A DEAL

This season, car buyers are in the driver's seat

Last September, Irvine (Calif.) car dealer John B. T. Campbell III had to beg Detroit to send him more vehicles. Even on overtime, auto makers couldn't keep up with runaway demand. Fast-forward a few months. Interest rates surged, confidence flagged, and in January, the bottom fell out. "All of a sudden, we were buried in cars," Campbell says. "I told Ford: Don't even think of sending us a single car for 90 days."

Now, on the eve of the 1996 model year, dealers say the feast-or-famine market has leveled out. "After a dreadful spring and a muddle-through summer, I would say we're in a recovering fall," says John Casesa, auto analyst at Wertheim Schroder & Co. Consumer demand is reviving a bit, and analysts say U.S. light-vehicle sales should reach 14.7 million units this year, down modestly from 1994's 15.1 million pace. For next year, even once-bearish prognosticator Lincoln Merrihew at DRI/McGraw-Hill is forecasting an increase to a 14.9 million sales rate. The supply side of the picture also is brighter: Detroit, chastened by a midyear glut of unsold cars, has slashed fourth-quarter production plans by 5.7%.

**GIVEBACKS.** Merrihew figures the situation in autos bodes well for the U.S. economy overall. A more torrid recovery in sales—which would strain supplies of parts and raw materials—might help rekindle inflation. The current prognosis, he says, supports the view of many economists that the Federal Reserve can continue to engineer a soft landing to moderate, sustainable economic growth.

One nagging worry: With the average price of a new car now hovering just below \$20,000 up about \$3,500 since

**EUROPE** From a small base, BMW and Mercedes have made big gains with lower-priced models,



including BMW's new 318ti hatchback. A big question: Can Volkswagen come back? Europe's U.S. market share has stabilized at about 3%.

1990, many executives fear a looming affordability crisis. Says G. Richard Wagoner Jr., GM's president of North American operations: "We believe affordability is a big issue."

To soften the blow, and reignite demand, auto makers have cushioned price hikes with big cash rebates and tempting lease deals. These days, 32% of all U.S.

auto sales are leases, many bargain rates, up from 27% year ago, says Art Spinella, CNW Marketing in Bandon, Or. And Infiniti had to resort to \$7,000 rebate this summer jump-start sluggish sales of its Q45 luxury sedans. Even Europe's BMW and Mercedes no routinely plug cut-rate leases.

For 1996, it's going to take more enticements, even on ne

models, to keep sales up. Laments Russell M. Darrow Jr., the West Bend (Wis.) owner of dealerships selling Chrysler and Japanese brands: "The incentive turned it into a buyer's market."

How much are buyers calling the shots? Even Chrysler Corp., the stubborn holdout in leasing, has caved. This summer, it began offering \$299-a-mon

## NEW MODELS! TERRIFIC BARGAINS!

*Demand may be reviving, but lease deals and rebates are taking a bite out of carmakers' bottom lines*



**▲ GENERAL MOTORS** new Saturn subcompact is its only significant new model. Next year is another story: GM has about a dozen new vehicles coming. Until then, market share, which has fallen 32%, may continue to decline.

DATA: COMPANY REPORTS



es on its popular Jeep Grand Cherokee. Now, Chrysler plans to slap attractive leases on its fast-selling new Dodge Ram and Plymouth Voyager minivans. Concedes Chrysler President Robert A. Lutz: "A year ago, we would not have contemplated introducing the minivan with a lease deal."

Detroit knows all these giveaways will reduce profits. The steep costs of launching new models—

the lost output and sales during changeovers—will also be a toll. Chrysler's profits are suffering at least temporarily as the company introduces the next generation of its minivans. Ford Motor Co. faces an even bigger profit bite as it gears up new versions of

one of its biggest sellers: the Taurus family, F-series full-size pickup truck, and Escort subcompact, which accounted for 40% of its total U.S. sales last year. As a result, analysts expect Ford's North American auto unit to post a net loss for the third quarter. General Motors Corp., with few new-model launches to drag down profits, "will likely be the only one of the Big Three to show more than last year," says Casasa.

**REAR GUARD ACTION.** But GM's lack of new offerings will take its toll on market share, now at 32%. Not until the 1997 model year will it be able to tempt buyers with a dozen or so new vehicles, including an all-new Chevrolet minivan. Chrysler's own redesigned minivans

could help it add a bit to its 15% share. But Ford's 26% market share is likely to slip at least temporarily during its multiple model changeovers.

To try to keep its share of the market steady, Ford is working to woo diehard import owners to its 1996 lineup. It is mailing owners of rival Honda Accords and Toyota Camrys invitations to lease a 1996 Taurus for two years, or return the

**JAPAN** Plenty of new models are due, including a revamped Honda Civic and Toyota's new RAV4 compact sport-utility vehicle. The new cars, combined with cheap lease deals, could give Japanese car companies a slight gain in share from today's 22%.



car after six months if they don't like it. Plus, it is throwing \$250 cash offers at Taurus owners who lease a new model.

Japanese carmakers, meanwhile, are unveiling a new tactic to counteract their largely yen-induced \$2,000 to \$3,000 per-car price disadvantage: new vehicles engineered to cost significantly less. Honda cut the price tag of the 1996 Civic by an estimated \$800 per car. Nissan also has stepped up its efforts to squeeze costs out of models such as Infiniti's I30 entry-level luxury car. And Toyota Motor Corp. is pushing hard to build more vehicles in lower-cost U.S. plants. On Sept. 11, it an-

nounced it will begin building its T100 pickup truck, souped up with a V-8 engine, in a new North American plant by early 1999.

Detroit is fighting its own rearguard action to lower base prices. Both Chrysler's new minivan and Ford's new Taurus made antilock brakes optional rather than standard, for instance. Overall, Ford is raising its 1996 prices by an average of 2.5% on comparably equipped vehicles; GM by 2.7%; and Chrysler by 1.4%. The dollar's recent move over 100 yen has given Japanese car companies a slight breather, and AutoPacific Group Inc. analyst Christopher W. Cedergren estimates they will increase prices by only an average of 2% this fall.

So what's hot for 1996? Trucks and sport-utility vehicles still dominate. A slew of new sport-utilities, from Toyota's snappy little RAV4 to Nissan's revamped Pathfinder, will join the red-hot field. But even on these products, lease deals and rebates are likely. Splashy new models alone just don't spark sales as they once did. Shrugs Lutz: "People don't believe anymore that it's vitally important or prestigious to have the latest and the greatest." Car dealers such as John Campbell fervently hope he's wrong.

*By Kathleen Kerwin, with Bill Vlasic and Keith Naughton in Detroit and Larry Armstrong in Los Angeles*

\$760

▼ **FORD** America's best-selling car and truck—the Taurus and the F-series pickup—get updates. Related costs may leave Ford with a third-quarter loss in U.S. auto operations, and the company's market share, now 26%, may slip as it gears up.



\$1,035



▲ **CHRYSLER** The new Sebring convertible and a new minivan are causing a stir. Chrysler hopes the cars will light a fire under weak demand and boost its market share above the current 15%.



## REAL ESTATE

# CALL IT THE GREAT WALT WAY

Disney lays claim to Manhattan with a rash of real estate deals

As a youngster growing up on New York's Park Avenue, Michael D. Eisner got hooked on Broadway. Starting with *Oklahoma!* at age 2, each of young Michael's birthdays was celebrated with a trip to the theater. Now, five decades and an entertainment empire later, Walt Disney Co.'s chairman seems intent on reclaiming a piece of his former haunt.

As part of a group headed by Chicago investor Sam Zell, Disney is bidding to own a piece of famed Rockefeller Center, complete with its ice-skating rink and storied Radio City Music Hall. Zell and Disney, facing a rival bid from Goldman, Sachs & Co., may not end up with the property at all. And as investments go, this is small potatoes for Disney: Zell puts its stake in his \$250 million takeover at roughly \$25 million—that's one-quarter what the company spent on its new Indiana Jones thrill ride at Disneyland. But the strategic and psychic value of acquiring yet another Disney showcase could go way beyond the paltry sum involved.

**EXPANSIVE VISION.** Disney already has created a broad beachhead in the Big Apple. This summer, it signed a long-term lease to operate the 90-year-old New Amsterdam Theater on 42nd Street just off 7th Avenue. Now, after pressuring the city and state to provide low-interest loans for 75% of the costs, it is directing a \$34 million renovation of the property. It has persuaded AMC Entertainment to open a 25-screen film complex down the block and has the option to sell time-share apartments in a \$303 million hotel and entertainment site across the street.

Nearby, a Disney Store is scheduled to open next year. Another is going up

on Fifth Avenue. Brokers also say Disney is looking into leasing a retail space in the World Trade Center. And with its deal to acquire Capital Cities/ABC Inc., it will inherit Cap Cities' headquarters in New York—a prime property. "This is a substantial number of commitments they are making," says Mary Ann Tighe, executive managing director of real estate brokerage firm Edward S. Gordon Co. and a board member of a nonprofit organization overseeing the 42nd Street renovation. She figures Disney has

committed \$100 million to New York real estate so far.

Why would Eisner, whose troops are scurrying to complete the company \$19 billion merger with Cap Cities, bother with these relatively minor projects in New York? The answer may lie in his expansive vision of Disney's role in the entertainment business. "People have to need to get out of their homes and find live entertainment," he told *BUSINESS WEEK* recently, "and if they venture out we intend to be there."

**RADIO CITY RULERS?** That's why Disney bought pro hockey's Mighty Ducks of Anaheim and has an option to buy baseball's California Angels. It's why the company launched *Beauty and the Beast* on Broadway last year and plans by 1997 to launch a new stage show a year in New York. Among the possibilities: *Mary Poppins*, *Pocahontas*, and a children's version of the opera *Aida*. Already, *Beauty*, which is playing to sellout crowds in Broadway's Palace

Theater and in Los Angeles, Toronto, and other cities, is a major profit center.

Disney is no stranger to Radio City, where it opened its *Lion King* and *Beauty* animated films and where it annually stages its Christmas shows. As part of the Zell deal, the company has an option to pick up the management contract for the 5,874-seat venue and for the smallish Equity Theater nearby. Zell is counting on his partner's help in turning around money-losing Radio City. "Disney enhances the value of the center and makes it back to prominence," Zell says.

Disney executives deny that they are about to assume control of Radio City. But there is a precedent for such a move: A few years back, Disney took over the dilapidated El Capitan Theater in Hollywood and invested \$16 million in an upgrade. Today, the El Capitan shows only Disney movies, with stage shows as regular

events. There are other signs that Disney thinks such a strategy is smart. Realtors in Chicago say Disney also is considering upgrading that city's Chicago Theater for use in promoting Disney movies.

Still, Disney executives say the role in Zell's deal is little more than



## MICKEY ♥ NY

Disney is in on the Rockefeller Center bid—and is fixing up 42nd Street's New Amsterdam



investment. "We needed a place to test the cash that this company proposes," says Stephen Bollenbach, Disney's chief financial officer, "and this looks like a good bet." And Disney has largely pulled back from other real estate investments. In 1987, it sold off its expansive Arvida real estate development unit, choosing instead to concentrate on far more modest time-share

communities in Hilton Head, S.C., and Vero Beach, Fla., as well as on Celebration, its residential village in Florida (box).

For now, Disney's New York presence seems slightly incongruous. Looking at the desolate scene around the sooty New Amsterdam, it's hard to imagine the Disneyfication to come. A nearby shop sells Harley Davidson and

heavy metal T-shirts, and down the block The Nugget advertises "Live Girls. 25-cent peep-show" in neon lights. These no doubt are not the Broadway memories of Eisner's youth. But even in Times Square, Disney's coffers could work some very fast magic.

*By Ronald Grover in Los Angeles, with Suzanne Woolley in New York and Richard A. Melcher in Chicago*

## A THEME PARK YOU CAN LIVE IN

No one wears mouse ears, and there's no pixie dust in the air—none you can see, anyway. Still, Celebration, Fla., a new housing development 15 minutes from Orlando, is unmistakably a Walt Disney production. It's immaculate, it's high-tech, and it's Middle America. "It's like living in a Norman Rockwell painting with all the modern technology," gushes visitor Patricia Gorman.

In mid-August, Disney unveiled plans—and a few model-home facades—for its 4,900-acre development, a vision hatched long ago by founder Walt Disney and the product of nine years of work by dozens of architects, town planners, and consultants. The plan: a self-contained village, modeled after pre-World War II Southeastern towns, featuring specific architectural styles and shopping, learning, and recreation areas.

While such all-in-one projects have been undertaken before, says architect Andres Duany, Disney "will give it a corporate imprimatur." Indeed, Celebration will be rooted in six architectural standards, from colonial to Mediterranean, all including wide front porches with garages banished to the rear. Builders must follow "pattern books" designating myriad specifications, from ceiling heights to front detailing. "The project is so canned, there is no creative crossover," grouses Orlando architect John Henry.

Canned or not, rumors of Disney's plans generated more than 2,000 inquiries before the preview center even opened; when it finally did,

4,000 visitors appeared in the first weekend. Terry and Beverly Neff were so impressed, they put their home in nearby Hunter's Creek up for sale the very day of their visit—even though the first of Celebration's homes won't be ready until mid-1996. Its first phase will include 350 houses, starting at \$127,000 for a 1,300-square-foot townhouse, and 123 apartments for rent.

Much of Celebration's appeal has to do with its approachable, human

date kids from pre-kindergarten through 12th grade. Disney consulted five universities, contributed \$11 million in land and capital, and will spend \$9 million more for teacher training and other enhancements for the school, which is being built and operated by Osceola County. Next door, at the planned Celebration Teaching Academy, teachers will learn innovative teaching methods. A fiber-optic link will connect the school, health center, and homes.



**FOR SALE:**

A 1940's-era environment, with Mickey and Goofy just down the street. Townhouses starting at \$127,000; "cottage homes" \$150,000 to \$200,000. School and health center, plus golf course, bike paths, and shopping. Pixie dust not included.

quality. Anchoring the mix of apartments, townhouses, and single-family houses will be a "town center" with shops, a bank, and a two-screen cinema. Bike and walking trails, parks, and an 18-hole public golf course will provide recreation. Next to a separate office center, called Celebration Place, will be Celebration Health, a health-and-fitness center focusing on wellness programs.

Flanking the town center, a public school will accommo-

For all this, Disney is charging \$90 to \$100 a square foot, roughly 30% more than homes command in surrounding communities. The prices put off some would-be Celebrators: "For New Jersey, they're not bad, but for here, they're on the high side," says Doug Samuel, who is moving to the area from the Garden State. Celebration officials, though, say prices are comparable when all of the extras are considered. Seven-year-old Colleen Gorman puts her finger on the biggest extra of all. "I like being close to Disney," she says. Many of the grownups here agree.

*By Gail DeGeorge in Celebration, Fla.*



## EXECUTIVE SUITE

# AT IBM, THE GREAT SHRINK-DOWN MAY BE OVER

With a new management team, the focus shifts to growth

**F**or a time, IBM Chief Financial Officer Jerome B. York was just what the struggling computer giant needed. In a little more than two years, the blunt-talking executive engineered a balance-sheet turnaround by relentlessly slicing corporate fat. Then, on Sept. 1, he dropped a bombshell: He resigned to become vice-chairman of Kirk Kerkorian's Tracinda Corp. and join its bid to take over Chrysler Corp. York acknowledges he's leaving IBM just as Chairman Louis V. Gerstner Jr. is making a major strategic shift, from York's no-holds-barred cost-slashing to a new focus on boosting revenue. "Lou's charter is, at this point in time, certainly the opposite [of mine]," York says.

That change in emphasis is largely behind what's shaping up as a major management shuffle at IBM. To replace York, Gerstner named longtime colleague G. Richard Thoman as CFO, yanking him off the as-yet-incomplete task of turning around Big Blue's struggling PC business. Gerstner also moved four executives up the ladder. The big surprise: Longtime IBM executive Robert M. Stephenson, unknown outside the computer giant, was given the high-profile job of running the PC business. What's more, IBM shuffled executives in its troubled software business. In all, nearly a dozen executives changed jobs.

**SOFTWARE CZAR.** Meanwhile, Gerstner has been quietly bolstering the ranks with outsiders. The latest example: Gian Carlo Bisone, lured from rival Compaq Computer Corp. to be software marketing chief. Up and down the ladder, Gerstner has recruited scores of executives to run everything from PC manu-

facturing to high-level consulting units. Since April, 1993, when Gerstner took over, 12% of IBM management has come from places such as Black & Decker, Booz Allen, NEC, Citibank, MCI Communications, and Compaq. "I'm sorry to see York go, but Gerstner does seem to be building a strong team," says William Milton Jr., an analyst with Brown Brothers Harriman & Co.

## SHUFFLING THE DECK



◀ **GIAN CARLO BISONE**, 48, general manager of software marketing. Strength: an ex-Compaq Computer exec with global marketing expertise.



▶ **ROBERT STEPHENSON**, 57, senior vice-president and PC chief. Strengths: no-nonsense attitude and ability to carry out existing strategy.



◀ **RICHARD THOMAN**, 51, chief financial officer. Strengths: longtime Gerstner confidant, rich international experience, has run several IBM businesses.

▶ **DAVID THOMAS**, 46, general manager in charge of North American sales. Strength: well-respected by IBM's sales force.



◀ **JOHN M. THOMPSON**, 52, senior vice-president and top software exec. Strengths: analytical skills, willingness to bring in outside people and suppliers.

▶ **JOHN W. THOMPSON**, 46, general manager of IBM's Personal Software Products Div. Strength: has worked with companies developing software for IBM.

Gerstner's main goal: To shift IBM's mix of skills from old-line mainframes and minicomputers to high-growth businesses such as networking, software, and services. That job is far from complete, as became obvious on Sept. 13 when IBM stock sank 3% to 94%, on the news that mainframe delays would hurt third-quarter earnings.

Gerstner's latest top-management picks are executives he thinks can produce greater growth. As head of North American sales, Stephenson helped streamline the sales organization, estab-

lish industry-specific sales units, and devise a compensation plan that boosts PC sales dramatically. David M. Thomas, who once headed IBM's successful AS/400 minicomputer business and recently ran Asia/Pacific sales, now gets the North American sales job.

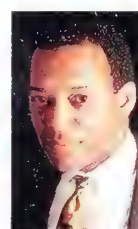
Bolstering IBM's critical software business is another key element of the shakeup. Software units contribute \$1 billion a year in revenue and an estimated \$2.5 billion in IBM profits. But those numbers have been slipping this year. So in January, Gerstner made experienced troubleshooter John M. Thompson IBM's software czar—its first. In addition to bringing in Bisone, Thompson shook up the troubled OS/2 software unit, moving in longtime marketing executive John W. Thompson.



John W., who is not related to John M., has been working to expand IBM's stable of independent software developers.



**GLOBAL SAVVY.** The man could be another big asset, analysts say. He has worked with Gerstner for 23 years in various capacities. Moreover, he ran several IBM businesses, including PCs. And, he was the first IBM CFO with a heavy dose of international experience—an area where the company already does 62% of its business and one that Gerstner is stressing.



At IBM, cost-slashing remains an important goal. To make room for new recruits, the company has cut workers in administration, finance, and marketing. Now, analysts expect to launch a new round

of cuts in its North American work force—anywhere from 6,000 to 10,000 employees—by the end of this month. The cuts will allow Gerstner to add a substantial number of employees in fast-growing businesses, while keeping employment at around 215,000 to 220,000, analysts say.

Now, if all those new managers will just lead the way, maybe IBM could get on to the next phase of its recovery—revenue growth.

By Ira Sager, with Amy Cortese, in New York



# RAWL IN THE COCKPIT T USAIR

the board takes a tough stance on unions, the CEO bails out

For Seth E. Schofield, the breaking point came Friday afternoon, May 28, in the winless eighth-floor boardroom of USAir Inc.'s headquarters in Arlington, Va. Months of negotiations with unions to reduce sky-high labor costs were going nowhere. As chief executive, Schofield had coffee with union representatives while discussing the terms of a new contract with the Air Line Pilots Assn., Schofield's mood suddenly darkened, say sources who attended the meeting. "We are in an impasse," he claimed. "We just can't do it."

Five weeks later, on Sept. 6, Schofield abruptly announced his resignation, effective as soon as a successor is installed. His departure shocked the industry: The executive has been widely credited for making USAir profitable despite two fatal air crashes, union strife, and a gloomy forecast of the company's future by its own accountants.

**FRESH LEGS.** Under Schofield, 56, the nation's sixth-largest airline has indeed made gains. For USAir's directors, however, "it's only a job half done," says board member John W. Harris, president of a real estate development firm. Soon after the union talks broke down, Schofield and directors agreed that he would step down for the good of the airline. "The highly visible and drawn-out negotiations with the unions just didn't work," says a former board member.

More important, few of USAir's diverse and fractious interests were happy with Schofield's progress. British Airways PLC, which holds three board seats and 24.6% equity, wanted to see a much tougher



**SCHOFIELD:** His exit shocked the industry

stance with the company's unions. Investor Warren E. Buffett, forced to write down his Berkshire Hathaway Corp.'s stake in the airline by \$270 million, wasn't any more sanguine. Union officials and other sources say the boardroom had grown tense in recent months.

Schofield declined to discuss his resignation; a USAir spokesman said only that the board wanted "fresh legs." At one time, though, the airline's board appeared to judge Schofield as well up to the task. He came into the job in mid-1992, after 35 years with the carrier, and developed an ambitious plan to cut \$1 billion a year from expenses. Progress was slow. Then, earlier this year, Schofield managed to strike tentative pacts with each of the airline's unions. After five straight years of losses, USAir reported a \$112.9 million second-quarter profit. It's now

poised to make money for the full year.

But the sunny financial outlook only played against Schofield. Union leaders questioned whether they still had to concede work rules and wages for a company that was suddenly profitable. Led by the pilots, they pushed for seats on USAir's board, plus a stake in the company, in exchange for \$2.5 billion in givebacks over five years. They pressed, too, for British Air and Buffett to accept lower dividends on their preferred stock.

**BUFFETT BEEF.** Meanwhile, British Air was angling for an agreement allowing it to strike partnerships with other U.S. airlines, a move Schofield and the unions both opposed. Neither British Air nor Buffett would accept the dividend cuts. And British Air balked at putting workers on the board. "We disagree with it in principle," British Air Chairman Sir Colin Marshall said in May. "But we must wait until we see the deal in full before making any decisions."

Schofield was caught in the middle. It didn't help that Buffett, disenchanted after seeing the value of his USAir stock plunge 75%, announced in March that he and Berkshire Hathaway Vice-Chairman Charles T. Munger would step down from the board in November.

Now, despite USAir's relative financial health, some unionists fear the

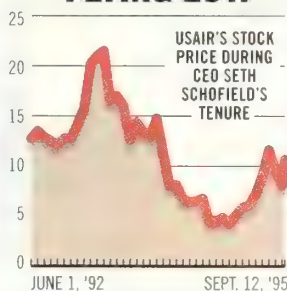
worst. With Schofield and Buffett leaving, "British Air is the only one left standing," says one negotiator, likely pointing USAir toward more labor war. Indeed, BA's Marshall, who is helping to lead the search for Schofield's replacement, probably will favor someone who will take a hard line in union talks. Two possible successors are former United Airlines

chief Stephen M. Wolf or Hollis Harris, who headed Delta Air Lines.

British Air must decide by the end of January whether to extend its option to buy more of USAir's stock. The airline surely could use more capital. But BA has said it won't increase its stake unless the carrier lowers labor costs. And the unions aren't budging. To investors, the scenario must seem depressingly familiar. Schofield's departure, ultimately, may not solve any of USAir's problems.

*By Christina Del Valle in Washington*

## FLYING LOW



▲ DOLLARS  
DATA: BLOOMBERG FINANCIAL MARKETS

Under Schofield, USAir has made big gains—despite two crashes, union strife, and a gloomy financial forecast



## THE FED

# SO MANY SEATS, SO LITTLE ROOM TO MANEUVER

The GOP won't make it easy for Clinton to fill Fed vacancies

Every President up for reelection should be so lucky: The economy seems headed toward solid growth through November, 1996. What's more, Bill Clinton has an opportunity in coming months to influence economic policy by filling three of seven seats on the Federal Reserve Board—including the powerful chairmanship. Funny, then, that the President's advisers are far from gleeful about this stroke of good fortune.



flation, and the markets could well react negatively if he gets the boot. "Nominating anyone besides Greenspan is a risk for the Administration," warns Senator Connie Mack (R-Fla.), chairman of the Joint Economic Committee. "The Administration should be careful about politicizing the Fed."

White House aides say Clinton considers Greenspan too hawkish on inflation. Given the choice, the President

not act on it," says Senator Robert Bennett (R-Utah).

Two outside possibilities for chairman: William J. McDonough, president of the Federal Reserve Bank of New York, and his predecessor, E. Gerald Corrigan. But they don't know Clinton well, and both are inflation hawks. "Neither is better than keeping Greenspan," says a former Fed official.

**RATE DEBATE.** As for the other seats, finding nominees suitable to the GOP is tough. The White House preemptively yanked its first choice for the open F seat, Administration economist Alicia H. Munnell, after Senate Republicans complained that she is too liberal. Choice No. 2, American Stock Exchange President Richard F. Syron—former president of the Boston Fed—passed on the job. Current candidates include First Chicago Bank's chief economist

James E. Annable Jr., First Chicago President Leo F. Mullin, and Harvard University economist Benjamin M. Friedman. But both Mullin and Friedman seem to be holding out for the vice-chairman's job.

Presidential aides involved in the search say Greenspan could seal Clinton's support with further rate cuts to help sustain the expansion through the election. The White House wants the Fed



The problem: The Republican-controlled Senate is vowing to play hardball over the Fed vacancies. GOP opposition already has torpedoed a potential candidate to replace former Governor John P. LaWare, whose seat has been vacant since March. Now, Republicans are threatening to exercise their veto power when Vice-Chairman Alan S. Blinder's term expires on Jan.

**THE GOVERNORS** Blinder (left) and Greenspan end their terms soon; the seat held by LaWare (top) has been open for months

would prefer someone who shares his philosophy—and would be more beholden to the White House. But Clinton has few alternatives. Treasury

Secretary Robert E. Rubin would have the best shot at Senate confirmation, but he does not appear interested. Promoting Blinder would meet with resistance from Wall Street and Hill Republicans, who view him as an inflation dove. If passed over for the top job, Administration officials believe Blinder will return to Princeton University.

But given Clinton's dearth of options, Greenspan & Co. may call that bluff. With the economy showing signs of recovering from its summer swoon, a number of Fed officials are reluctant to cut rates anytime soon—and then only if the Administration and Congress deliver on their vow to slash the federal deficit.

Some advisers want Clinton simply to name his choices and campaign against the GOP for playing politics with the Fed. But that won't help the economy or the President's reelection chances. Before it's all over, Clinton may just find himself declaring his devotion to Alan Greenspan.

By Dean Foust in Washington



ate Banking Committee Chairman Alfonse M. D'Amato (R-N.Y.).

**FEW ALTERNATIVES.** GOP lawmakers are all but demanding that Clinton reappoint Greenspan, a conservative Republican, to a third four-year term. Greenspan is popular on Wall Street, which believes he has delivered the perfect mix of moderate growth and low in-

Other Clinton economic aides—National Economic Council Director Laura D'Andrea Tyson and Deputy Treasury Secretary Lawrence H. Summers—lack the stature to serve as Fed boss, say Republicans. "If they send us any name other than Greenspan, we just might





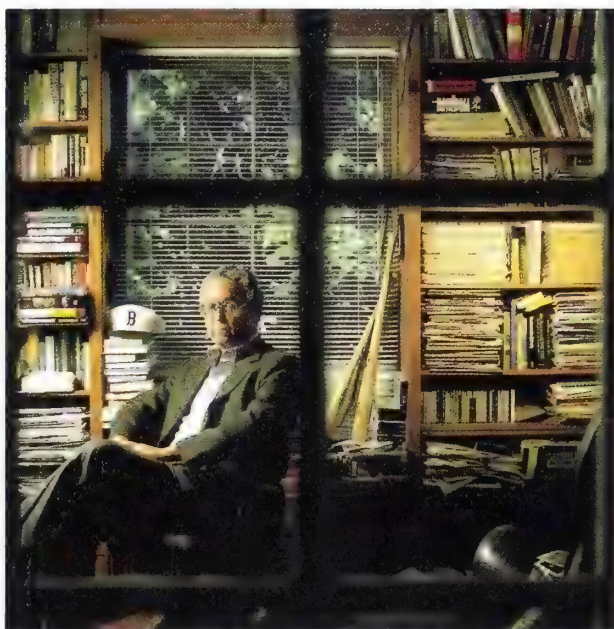
# THE LONG KNIVES ARE OUT FOR BILL GOULD'S NLRB

But the labor board's chief isn't cowed by House budget threats

political savvy he may be short on. But say this for Gould: He has guts. As congressional allies brandish their get-cutting knives, dozens of many regulatory agencies are scurrying to placate Republican constituents in the business community. William B. Gould Jr. As chairman of the National Labor Relations Board, Gould has continued his agency's aggressive pursuit of employers who violate federal labor law.

Now, the NLRB's fate is in the line. In mid-July, employers unhappy with agency rulings against them prodded House Republicans to slash the board's \$176 million annual budget by 30%. While a Senate subcommittee voted on Sept. 13 to maintain funding at current levels, agency insiders still expect the board to wind up with heavy cuts when the bills are reconciled in October. Given a 30% reduction, says Gould, the 37-year-old agency would be forced to close half its 52 field offices and lay off almost a third of its 2,000 staff—atop the 900 positions eliminated since 1980.

**WART CRITIC.** The GOP-led Congress might have reached this draconian juncture anyway—but Gould's no-punches-retained approach hasn't discouraged the attack. His NLRB has issued 101 injunctions this year, triple the number of prior years. It also has taken unusual measures to curb law-breaking employers, such as a recent ruling that textile maker Fieldcrest Cannon Inc. must let agency officials read workers a cease-and-desist



sist order against the company (table).

One action in particular triggered the attack on the NLRB's budget. In June, the board authorized an injunction against Union Pacific Corp.'s Overnite Transportation Co. trucking unit, after finding it had violated workers' rights during organizing drives by the International Brotherhood of Teamsters. Overnite settled the case this summer, avoiding the injunction. But Union Pacific and Overnite launched an intense lobbying campaign on the Hill. They persuaded Representative Jay Dickey (R-Ark.), a member of a House Appropriations subcommittee, to recommend the drastic budget cuts. Subcommittee head John Edward Porter (R-Ill.) opposed the action, saying: "You don't cut judicial bodies because they make decisions you don't like." Still, Overnite's lobbying carried the day.

Gould, a Stanford University labor law scholar who took over the agency early last year, vows not to back down.

"I took an oath to enforce the law," he says. "I couldn't look at myself in the mirror if I cringed every time political pressure comes along." An expert on racial discrimination in the workplace as well as sports labor law—and a longtime baseball arbitrator—Gould has been outspoken in his support for labor law reform, much of which is anathema to employers. He disagrees, for instance, with a 1938 U.S. Supreme Court decision legalizing permanent replacement of striking workers.

**ANTIBUSINESS?** Some management lawyers believe he's pushing an antibusiness agenda. To combat illegal management actions during organizing drives, for example, the NLRB has taken to singling out top executives who violate the law. A recent board complaint against Columbia/HCA Healthcare Corp. alleged that Chief Operating Officer David T. Vandewater "threatened" nurses and vowed not to negotiate with them even if a majority voted in a union. Columbia says Vandewater's remarks were taken out of context.

In fact, however, Gould's rulings adhere closely to precedent, says Andrew M. Kramer, a Jones, Day, Reavis &

**GOULD:** "I took an oath to enforce the law" Pogue lawyer who represents Bridge-stone Corp. in its dispute with rubber

workers. In a recent case involving an employer charged with limiting access to union organizers, says Kramer, "Gould criticized the Supreme Court ruling on the issue in his book. But when the case came before him, he said he had to follow the court and ruled for the employer."

No matter: Gould has made plenty of enemies among companies accustomed to the less vigorous enforcement that prevailed under Reagan-Bush rule. Ironically, though, the House-proposed cuts to the NLRB could end up hurting employers as well as unions. "A 30% cut is a mistake for management because the time needed to resolve cases will stretch out," says Dennis M. Devaney, a former NLRB board member whose law firm represents Caterpillar Inc. And the threat of a budget crisis won't likely cow Gould. It may just make him even tougher.

By Aaron Bernstein in New York, with bureau reports

On the  
Warpath

Recent enforcement  
actions by the National  
Labor Relations Board

**COLUMBIA/HCA HEALTHCARE** Its chief operating officer was alleged to have threatened unionizing nurses; now the NLRB says the union should be recognized even though it lost the election

**FIELDCREST CANNON** The textile maker must pay \$2 million in back wages, and a human resources vice-president must attend employee meetings at which agency officials will read aloud a cease-and-desist order

**OVERNITE TRANSPORTATION** The trucker agreed that more than 900 managers would face federal-court contempt charges if they violate workers' rights related to union organizing

DATA BUSINESS WEEK



## B-SCHOOLS

### KIM CLARK MEANS BUSINESS NOW

He almost quit Harvard as an undergrad. Today, he's a dean

**K**im B. Clark vividly remembers arriving at Harvard College as a freshman in late summer of 1967. To earn his financial-aid benefits, he spent his first two weeks cleaning undergrad dormitories and stumbled through the rest of his first year overwhelmed by the school's demands. "I was clueless," he says. "You could not have found someone who was less prepared to come here than me."

Lucky thing he eventually stuck it out. Nearly three decades later, Clark is preparing for yet another cleanup role—this time as the new dean of Harvard's business school. On Sept. 11, the university named the soft-spoken professor of technology and operations as successor to John H. McArthur, who had held the post for 15 years.

Clark's appointment, which is effective Oct. 1, comes at a critical juncture. In recent years, Harvard has slipped in national business school rankings, including *BUSINESS WEEK*'s. The B-school has lagged rivals in updating its basic curriculum. Its highly paid graduates also bemoan what they consider an unresponsive administration. Some MBAs even complain that they lack basic accounting or finance skills when they graduate.

Clark arrives in time to lead a recently begun overhaul of the school's MBA program and to preside over its switch to a 12-month school year. "He's smart and balanced," says Thomas S. Murphy, chairman of Capital Cities/ABC Inc. and head of Harvard's visiting committee. "He knows where the school should go, and he'll take it there."

**"DOWN TO EARTH."** Clark, 46, is widely respected for both his scholarship in manufacturing and his witty, self-deprecating style. Unlike McArthur, who wasn't known as an effective speaker, Clark is articulate and at ease with outsiders, whether in press conferences or classrooms. Says Steven C. Wheelwright, a Harvard prof and jogging

partner: "He's a very comfortable guy, just relaxed and down to earth." He's also a bit of a straight arrow: A devout Mormon who neither drinks nor smokes, Clark "is not much fun at a party," laughs a friend.

Clark's rise to success was far from foreordained. His father, Merlin, a former advertising manager for agriculture and ranching magazines, was the first in his family to earn a college degree. Kim Clark nearly faltered trying



### Clark's challenge: Restoring the influential business school's flagging reputation

to become the second. Far from a stellar student, he admits he got into Harvard largely thanks to the recommendation of an influential alum from Spokane, Wash.

Homesick and dazed by the premed courses he initially loaded up on, Clark left Harvard within a year to become a missionary for the Mormon Church at 19. After a two-year stint in Germany, Clark returned to Utah and Brigham Young University, where he met his future wife, Sue. Within a month, they were engaged, and they married shortly before he returned to Harvard in 1971 as an economics major.

Better grounded this time around, Clark earned his bachelor's degree three years. He stayed at Harvard to earn his master's degree and doctorate before joining the business faculty in 1978. "I knew I liked to teach, and knew I liked to talk," says Clark. "I thought, 'What a great idea: They actually pay you to do this.'"

**SCOUTS AND HOOPS.** At the business school, Clark successfully carved out a niche in operations and technology by studying the development of new products and innovation. At home, he is actively involved in his church and in the lives of his seven children. He spent three years as a Mormon bishop counseling married couples, was Boy Scout master for a church-affiliated troop, and spends Saturdays coordinating a boys' basketball league.

At the B-school, Clark says he wants

#### KIM B. CLARK

**BORN** Mar. 20, 1949, Salt Lake City

**EDUCATION** AB (1974), MA (1977), and PhD (1978) in economics from Harvard

**ACADEMIC SPECIALTY** New-product development, with heavy focus on auto industry

**FAMILY** Married to Sue for 24 years; seven children, aged 10 (twins) to 21

**PERSONAL** Devout Mormon, formerly church bishop; jogs; coaches kids' basketball

to speed up changes in the MBA program, more closely integrate the school's lucrative publishing operations by increasing faculty involvement in them, and more aggressively recruit and develop new, young faculty. "The major challenge I see here is to help to create an environment where we can attract very talented, creative people and where we can help them develop well," says Clark. "Yes, we're doing it, but we can do it better." For Clark, such a challenge is a long way from scrubbing undergraduate bathrooms.

*By Lori Bongiorno in Boston and John A. Byrne in New York*

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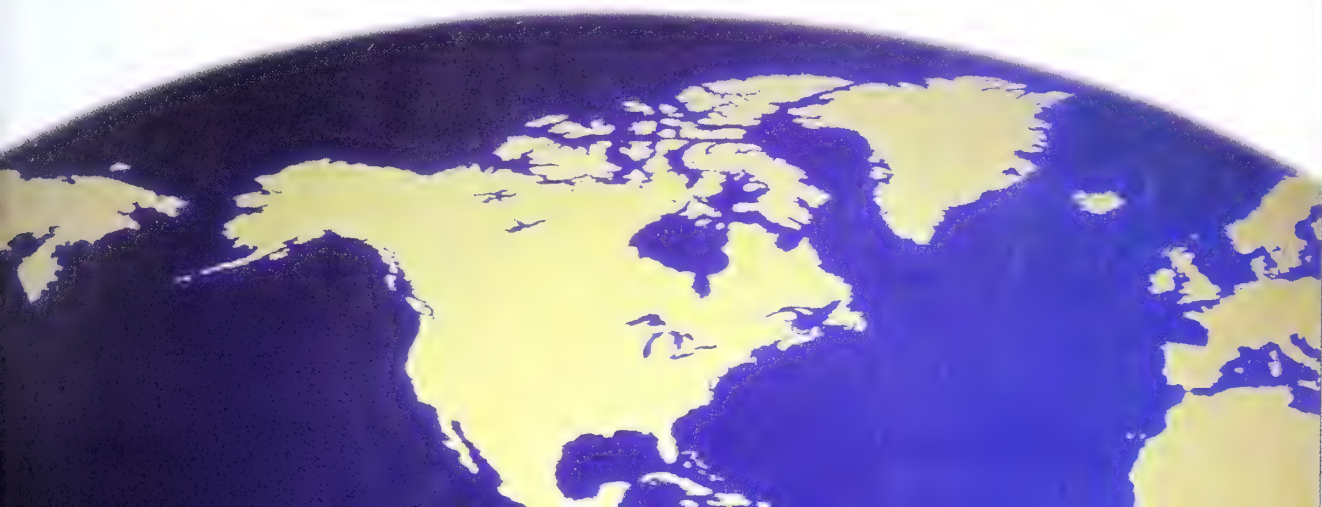
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## SOCIETY

### COFFEE A LA MODEM

At Internet cafés, skinny latte meets virtual reality

I'm well into my third caffe latte before I even think to look up at the clock. Whoops. I'm also into my third hour on the World Wide Web. This is getting to be a pricey Friday night at Cyber Java, a new Internet café in Venice, Calif. The guy peering over my shoulder shrugs. "I've seen much worse ways to spend \$7.50 an hour," he says.

True enough. It's also true that with a steady supply of joe, I could sit here and surf the Net all night. Cyber Java's six Pentium-powered computers share a direct, T1 Internet link, have big color monitors with videoconferencing capabilities, and are loaded with the necessary navigational software to turn the chaotic Internet into a brightly colored, easy-to-read multimedia experience. The best part? I'm not holed up in some office or crouched over my laptop at home. I'm in an actual café, with all the attendant social benefits. Cool music. A friendly, talkative Southern California crowd. And plenty of hot java.

**NEWBIE-FRIENDLY.** Welcome to another Internet café. These venues, unlikely combinations of food and computers, are taking the Net out of the realm of hardcore techies and into the hands of the public—neophytes and all. And since the first of these cafés appeared in San Francisco and Seattle some two years ago, the idea has caught fire. Three such sites have opened in New York since the start of summer, with more on the way. "Coffee and the Internet, what else interests our generation?" asks Rom Agustin, 29, Cyber Java's founder. His place opened its doors in July; he knows of half a dozen others due to open around Los Angeles by Thanksgiving.

Will this craze go the way of the fern bar? Maybe not. "Sushi bars were once a fad, but now a large part of the American population eats sushi," says Glenn McGinnis, 25, a co-founder of @ ("At") Café, a Manhattan bar/restaurant with 15 PCs jacked into the Net. He and others say the cafés perform a

service by giving people a place to learn about the Net in an unthreatening ambience.

Still, a business needs to turn a profit. And exactly how to make coffee and the Internet pay is problematic. Cafés and restaurants are notoriously hard to keep afloat anyway. Add the expense of state-of-the-art computers, high-speed dedicated Internet hookups (up to \$5,000 a month), and technical support, and it quickly adds up to a bundle.

As Internet cafés struggle to make ends meet, many are turning to consulting, says McGinnis. Companies all want to jump on the Internet bandwagon, but few know where to begin. That's when they approach café owners—mostly 20-something and technically savvy—for advice and help in setting up their World Wide Web pages.



**WHERE IT'S @:** East Villagers surf the Net

By Monday night, I'm back in the East Village at the @ Café. There's a decent clutch at the bar, and four or five folks in the back, surfing the Net. Sanae Foujita, in town from Okinawa, Japan, and Manhattan lawyer Philip T. Davies are having an online discussion with someone about, of all things, dating. I've already been to a dozen interesting nooks on the net, from the Small Business Administration's Web site to a former roommate's personal page. Not exactly a wild night, at least not in the East Village sense of the word. But it's far better than a solo trip down the I-way.

By Julie Tilsner in Venice, Calif., and New York

## BENEFITS

### THE BABYSITTERS CLUB

A business coalition spends big to upgrade dependent care

When Children's Courtyard opened a day-care center near Dallas last year, it was leery of hiring a big staff. But with IBM, Xerox, and Allstate Insurance pushing for top-notch care to serve their employees and willing to help cover costs, Courtyard President James D. Mills decided on a high teacher-to-child ratio. Even with fees 9% above average, the center was filled in six months. "If you put a high-quality product out there, people will seek you out," Mills says.

That's a lesson the American Business Collaboration for Quality Dependent Care (ABC) hopes to spread. Backed by 21 companies, including the three involved in Children's Courtyard, ABC was due to announce on Sept. 14 it would spend \$100 million over six years on child- and elder-care projects. That adds to more than \$27 million spent by ABC supporters since 1992 for such schemes as building day-care centers and money management training for the elderly.

**LEFT OUT.** The companies hope the investments will pay off in their employee recruitment, retention, and productivity. But ABC's impact should go far beyond the 21 companies leading the way. In the first phase, 156 businesses, government bodies, and nonprofits contributed to projects in 45 communities. ABC now plans to invest in programs it considers innovative and replicable.

The question: With the federal government set to slash child-care programs, can even this corporate investment make a dent? Helen Blank, director of child care at the Children's Defense Fund, figures House welfare reform proposals would cut child-care spending by \$7.6 billion over five years. Few argue that business should pick up the slack. But some raise concern about a growing gap between the haves and the have-nots. "What about the kids who are not in communities where these companies are focusing?" asks Faith A. Wohl, director of workplace initiatives at the General Services Administration. Likely, some will get left behind. But ultimately, ABC's dollars may move dependent care higher on the nation's agenda.

By Wendy Zellner in Dallas



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# In Business This Week

EDITED BY KEITH H. HAMMONDS

## THIS JUST WASN'T AST'S WEEK

FOUNDER SAFI QURESHEY IS perilously close to losing control of \$2.5 billion personal-computer maker AST Research. On Sept. 11, the company announced that revenues for the current quarter would be flat or down, and that it would post a net loss "significantly higher" than the \$40 million shortfall for the quarter a year ago. Analysts now predict that AST also will report a loss for the fiscal year ending next July. That could trigger a clause in its agreement with Samsung Electronics, which owns a 40% stake, which would give the Korean company management control. AST also an-

nounced the resignations of President James Schraith and two other senior executives and launched a search for a seasoned executive to run the company.

## UNCLE SAM WANTS YOU ... TO SAVE

HOW TO INCREASE AMERICANS' savings? The Competitiveness Policy Council has a modest proposal: issue tax refunds in the form of interest-bearing U.S. savings bonds. If taxpayers didn't cash them in, the \$85 billion in annual refunds could boost personal savings by 40%. The idea was contained in a report scheduled to be issued on Sept. 14. In it, the federal advisory council shied away from a subcommittee recommendation that the income tax be replaced with a tax on consumption that exempts all savings and investment income. Turns out the panel—which includes Clinton Administration economic adviser Laura D'Andrea Tyson—balked at endorsing an idea previously associated with Republican tax reformers.

## DUNKING A BASKETBALL STRIKE

WHILE BASEBALL ENDURES A summer of fan discontent, the National Basketball Assn. appears to have averted a similar fate. On Sept. 12, players voted against decertifying their union, an action proposed by such dissident stars as Patrick Ewing and Michael Jordan. Union reps the next day ratified a plan that would limit total player salaries to 48% of league-wide revenues, vs. 53% under previous pacts. Owners are almost certain to approve such favorable terms quickly. That would end the current lockout of players, allowing the NBA season to begin as scheduled on Nov. 3.

## HEADLINER: BRIDGET MACASKILL

## INVADING THE BOYS' CLUB IN FUNDS

Her predecessor tripled assets in seven years. Now, Bridget Macaskill, Oppenheimer Management's new chief executive, wants to pull the same trick in five. With mutual-fund assets becoming more concentrated in large firms, "it's going to be difficult for smaller companies to survive," she says.

The British-born Macaskill, 47, was named to head the nation's 18th-biggest fund company on Sept. 11. "She's a no-nonsense kind of person with good business sense," says Louis Harvey, president of Boston mutual-fund consulting

firm Dalbar. Macaskill came to Oppenheimer from St. Ivel, a British food distributor. Twelve years later, she is set to become one of the highest-ranking women in mutual funds. Her challenge: keeping a somewhat small player relevant in the

quickly consolidating business. Macaskill plans to continue broadening Oppenheimer's product line, adding global funds and acquiring new products. She'll also focus on marketing to women, who she says need to take better care of their own finances.

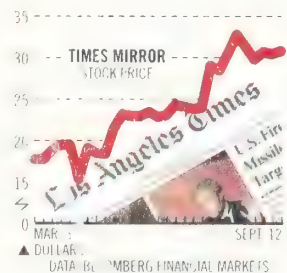
By Geoffrey Smith



## CLOSING BELL

## IRON WILLES

He closed *New York Newsday*. He sacked 700 at the *Los Angeles Times*. And on Sept. 7, Mark Willes shuffled top management at Times Mirror, ousting three senior executives. Wall Street loves his style: Times Mirror stock has soared nearly 70% since Willes was named president and CEO on May 1, to 30% on Sept. 13. Now comes the hard part: expanding the business after disbanding or paring electronic media, regional sections, Spanish-language editions, and other would-be growth vehicles.



## CHRYSLER AND YORK MAKE A DATE

IT MAY BE DETENTE IN DETROIT—or the opening salvo in the next war. Kirk Kerkorian's new right-hand man, Jerome York, has scheduled a summit meeting with senior Chrysler executives as soon as the week of Sept. 18, Chrysler insiders say. They'll have plenty to talk about—such as York's criticism that Chrysler doesn't share enough cash with shareholders such as Kerkorian. At least York, a former Chrysler CFO, wants to talk; Chrysler claims Kerkorian's camp rebuffed an offer last month to discuss strategy.

## 'OK': NOT OKEY-DOKE WITH COKE

IN THE END "OK" SODA WAS too hip for its own good. "OK" was Coca-Cola's gift to Gener-

ation X, complete with a toll-free phone line teens could call to hear grunge-talk about sodas and the meaning of life. Coke marketing chief Sergio Zyman once predicted "OK" sales would reach \$1 billion a year. But test-marketing indicated customers were confused by the drink's flavor, which some likened to the "suicide" drinks kids once concocted by mixing all the flavors at the soda fountain. On Sept. 12, Coca-Cola said it was pulling the plug.

## ET CETERA...

- UJB Financial will pay \$1 billion in stock for New Jersey rival Summit Bancorp.
- Ellen Hancock, once IBM top woman exec, will join National Semiconductor.
- Britain won't seek the extradition of former Baring trader Nick Leeson.
- Art Buchwald and a partner will get \$1 million to settle their Paramount suit.



EDITED BY OWEN ULLMANN

## WILL REPUBLICANS MAKE CLINTON THE EDUCATION PRESIDENT?

Education is one of those perennial issues that's wildly popular with voters yet never hits any hot buttons during Presidential campaigns. But 1996 may be the exception. Congressional Republicans, determined to balance the budget, are targeting virtually every federal education program from Head Start to college aid to the war on drugs in schools. At the same time, most GOP Presidential candidates are signing on to the Christian Coalition's crusade to strip Washington of any say over what goes on in the classroom. Topping the group's agenda: closing the Education Dept., providing vouchers for private schools, and allowing school prayer.

But the White House believes the Republicans are handing a winning issue to President Clinton, who's even picked up some support from GOP pals in corporate America, such as TRW Corp. and United Parcel Service Inc. "The information era and the knowledge-based economy are driven by education," says Education Secretary Richard W. Riley. "It's foolhardy to retreat now."

What has become a prominent campaign mantra for Clinton, who has been on a frenetic journey to classrooms across the country since Labor Day. At a recent roundtable with college students in Carbondale, Ill., he lashed out against the GOP for producing a balanced-budget plan that would "make the American people less well-educated."

**INITIATIVES.** To drive home the point, the President is engaging corporate chieftains, who worry that Republican cuts in education will make it difficult to maintain a highly skilled workforce. On Sept. 6, a small group of CEOs met with Clinton and promised to lobby the Senate to maintain \$372 million in Goals 2000, a program that provides money to states to raise achievement. States can adopt standards created by federally funded panels or develop their own. But critics argue that the feds should have no role in standards, even

voluntary ones, and the House has voted to end the program.

The CEOs—including Joseph T. Gorman of TRW, John E. Pepper of Procter & Gamble, Louis V. Gerstner Jr. of IBM, David R. Whitwam of Whirlpool, and Kent C. Nelson of UPS—helped lobby for passage of the bill last year. Now, they're writing to senators to save it. Gorman says he hopes business can "depoliticize" the issue "and get the facts on the table so that people understand how critically important this really is." Adds Nelson: "Public education is key...to our continued ability to compete."

Under such pressure, Senate Republicans are likely to restore some Goals 2000 funding. But the GOP still thinks the theme of government encroachment plays well on the campaign stump. GOP Presidential hopefuls stepped up the attacks at the Christian Coalition's annual convention Sept. 8-9 in Washington. Vows by Senate Majority Leader Bob Dole and his rivals to shut down the Education Dept. won the loudest applause. They also think calls for vouchers will woo voters who believe tax dollars are funding inferior schools.

The louder the cheering, the better, say Clintonites. They believe harsh GOP rhetoric will lead voters to conclude that Republicans don't care about education. Some proof: polls showing 80% of respondents oppose elimination of the Education Dept. The White House also is betting that most Americans will feel uneasy about GOP ties to the Christian Coalition.

In his fight for more education dollars, Clinton must be careful that he doesn't come off as a defender of the status quo who thinks every problem can be solved with more federal bucks and rules. The public rejected that approach last fall. But when it comes to education, the voters may yet give the President an A and send Republicans to the corner.

*By Susan B. Garland*



**CLINTON:** Allies even among GOP CEOs

## CAPITAL WRAPUP

### STATES' EUROPEAN WOES

While the Justice Dept. mulls whether to file antitrust charges against Microsoft Corp., European antitrustbusters are jumping in. At issue: Does the new Windows 95 software, which offers Microsoft's own online service, unfairly crowd out online and Internet-access competitors? The European Commission issued subpoenas to Microsoft rivals in August. Microsoft's competitors believe that EC law will be more receptive to their antitrust claims.

### TOOLING UP?

► Malcolm S. Forbes Jr. hasn't said so officially, but employees at the magazine bearing his name are betting that he will enter the Republican Presidential race. During a Sept. 8 company picnic at his Bedminster (N.J.) estate, the *Forbes* editor-in-chief hinted that he will turn over the reins of the family business to his younger brother, Timothy. The multimillionaire sees himself as the only true supply sider who may run. Company officials say a formal decision is imminent.

### SPLIT RANKS IN A TRADE SPAT

► The National Association of Manufacturers is caught in the middle of a nasty trade feud between Eastman Kodak Co. and Fuji Photo Film Co. NAM member Kodak wants the group to send a letter to U.S. Trade Representative Mickey Kantor strongly supporting Kodak's unfair-trade complaint against Fuji. But NAM balked at the urging of another member, Polaroid Corp., which fears Kodak's case may hurt its sales in Japan. Possible compromise: a tepid letter of support.

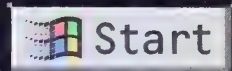


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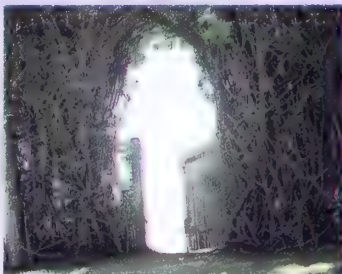


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## JAPAN

# TOKYO IS FINALLY GRABBING THE ECONOMY BY THE HORNS

A sudden burst of initiatives raises hope that a turnaround may be in sight

**T**his year has been a real bummer for Tokyo officialdom. A series of credit union collapses and Japan's first postwar bank failure have sent anxiety levels soaring. A new world competitiveness study by the Swiss International Institute of Management Development says Japan is falling behind the U.S., Singapore, and Hong Kong. And Japan's four-year economic slump has corporate leaders wailing for relief. "This downturn has gone on way too long," laments Toyota Motor Corp. Managing Director Fujio Cho.

While Japan's economic ills run deep, a surprising burst of economic and political activism is beginning to lift Tokyo's pervasive gloom. By any measure, it looks as if Japan is turning a corner. If policymakers' recent moves to restart and deregulate the economy gain momentum, a Japan that's increasingly linked to fast-growing Asian markets could even return to annual growth rates of 4%, some economists believe (table). **PARALYSIS FADES.** The battle to rejuvenate the economy is being fought on three fronts. This summer's currency-market interventions by the Bank of Japan, the U.S. Federal Reserve, and the German Bundesbank have pushed the yen back to its lowest point in a year, prompting exporters to raise profit estimates. The Bank of Japan's half-point cut in its discount rate, to 0.5%, on Sept. 8, has helped lift the Nikkei stock average 22% from this year's low. And odds are that the government soon will unveil \$100 billion in new spending.

There are also signs that Japan's damaging political paralysis may give way to assertive leadership. A shakeup within the pro-business Liberal Democratic Party, the biggest player in the three-party coalition gov-

ernment of Socialist Prime Minister Tomiichi Murayama, could lead the way. International Industry & Trade Minister Ryutaro Hashimoto (page 74), whose deft handling of the U.S.-Japan auto trade dispute won him celebrity status at home, is now considered a shoo-in to assume presidency of the LDP in a Sept. 22 leadership vote.

In general elections expected early in 1996, Hashimoto, 58, aims to return Japan's biggest party to uncontested power for the first time since 1993, when the LDP was ousted by renegade reformers. Hashimoto, a former Finance Minister, is expect-

ed to be sympathetic to corporate Japan's calls to use public money and tax breaks to bail out banks and halt the 60% slide in commercial-property prices since 1991. "The collapse of financial institutions has damaged confidence in the Japanese economy," he says. "What I have to do is restore the economy.... I will use any weapon I have."

But even under the current government, moves already under way should keep Japan from falling back into a recession. With the dollar's value expected

### SCENARIO 1

## Japan Transformed

Deregulation moves ahead

Yen depreciates as current account shrinks

Exports rise as competitiveness is regained

Corporate investment revives

Resolved bank crisis strengthens financial system

Long-term annual growth

4.0%

## Getting the Motor Started





rebound to 105 yen or higher, from in April, the economy may expand % this year and 1.6% in 1996. To get an back to its long-term growth potential of 3% to 4% will require more aggressive steps, however. That's why recent policy changes suggest there is hope.

**REPLENISHING RESERVES.** Take Japan's battered lenders, now saddled with an estimated \$800 billion in bad debt due to the collapse of the bubble economy. The yen is standing in the way of an economic recovery by keeping banks from increasing lending for everything from cars to homes. But with short-term interest rates at historic lows, banks are now getting a once-in-a-lifetime chance to replenish depleted equity reserves by borrowing from the money market at close to zero interest. Finance purchases of government bonds yielding 2.9%. On top of that, ready cash infusions by the Ministry of Finance (MOF) and Bank of Japan have averted widespread panic after runs on depositors at several big credit unions and the collapse of Hyogo Bank, a regional lender near Osaka.

The scares probably have softened public resistance to the use of taxpayer

als push through the tough measures needed for privatization, Japan could roar back. If not...

ers' money for further bailouts and raised interest in replenishing Japan's \$10 billion Deposit Insurance Corp., whose reserves have been wiped out by the recent banking failures. The MOF might also issue bonds to capitalize newly created "work-out" banks to assume the bad loans of weaker players. And it could set up something like the Resolution Trust Corp., the agency that bailed out U.S. thrifts. The Japanese version would assume and sell off assets of Japan's housing-loan corpora-

gross domestic product now to as little as 1% by 2000 is achievable.

The import surge is turning Japan's inefficient retailing sector on its head and offering consumers real savings. And, surprisingly, it's waking up Japan's high-technology sector. Intense price competition from Compaq, Apple, and IBM have spurred Japanese rivals such as NEC Corp. to make similar moves, sparking a boom in personal computer sales. Lower prices for cellular phones have demand soaring, and a raft of new

## The Ministry of Finance seems serious about bailing out the battered banks—and an alarmed public seems willing to pay for it

tions, or *jusen*, whose problem credits total \$60 billion.

The MOF's efforts to solve the banking problem are only one sign of economic reform. This year's import boom is also opening up the economy in historic fashion. Thanks to a wave of foreign products, Japan's current-account surplus plunged 15% in dollar terms in July. Indeed, most economists believe Hashimoto's goal of lowering Japan's trade surplus from 3% of

long-distance companies has shaved 50% off the average price of calls to the U.S. There is even talk of splitting Nippon Telegraph & Telephone Corp., the national phone company, into five independent units to spur competition.

Even more deregulation could take place. Some 40% of Japan's manufacturing output is micromanaged by 10,000-odd rules, many of which keep out foreign rivals and shield unproductive players. But even though Hashimoto believes "there is a lot more to do" to deregulate the economy, he may still be loath to throw open all the portals of Fortress Japan if it means the nation's 3.2% jobless rate will soar past 5%.

Nonetheless, Hashimoto—or any other leader—will continue to face heavy pressure from Washington to deliver measurable improvements in Japan's trade surpluses. That's likely to keep a fire under Japan to boost domestic spending, deregulate, and address critical questions. Will the country's high-cost manufacturers and bloated labor force eventually leave it a spent industrial giant with diminished growth prospects? Or will Japan endure the short-term pain of radical corporate overhauls and higher unemployment to emerge revitalized at home and abroad for the long haul?

The betting is that policymakers, invigorated by the economy's scary brush with bank failures and recession, are finally trying to lay the groundwork for revitalization. New political leadership could give that effort a tremendous assist—if Hashimoto chooses to rise to the challenge.

By Brian Bremner in Tokyo



### SCENARIO 2

## Japan's Secular Decline

Halfhearted deregulation keeps yen high

Production continues to move offshore

Unemployment approaches Western levels

Corporate investment remains depressed

Bad-debt woes carry on into next century

Long-term annual growth

1.0%

DATA: DRI/MCGRAW-HILL



## A TALK WITH RYUTARO HASHIMOTO

**W**ith his trademark cigarette holder, sideburns, and ink-black pompadour, Japan's Ryutaro Hashimoto mixes flair with a lifetime experience in the political trenches. After watching two reform leaders fail, voters seem to favor him to become Japan's next Prime Minister. Hashimoto, currently International Trade & Industry Minister, discussed Japan's future on Sept. 13 with *BUSINESS WEEK* International Managing Editor Robert J. Dowling and Tokyo correspondents Brian Bremner and Edith H. Updike in his Tokyo office.



**Q:** After four years of recession, Japan is said to be suffering a crisis of confidence. Do you agree?

**A:** The collapse of financial institutions has damaged confidence in the Japanese economy. And this is shown by the very miserable ratings from the international rating agencies and the extra premium that Japanese banks have to pay in money markets. Because of the Kobe earthquake and terrorism, the myth of the safety of Japan has also collapsed. This is a sad story.

**Q:** You are on the verge of becoming president of the Liberal Democratic Party and possibly Prime Minister. How would you suggest to change things?

**A:** I want voters to regain confidence in politics. I'm concerned about the very low level of voter participation. That is the main reason why I have challenged the leadership in the upcoming LDP election. There are many uncertainties right now in Japan. I would like to wipe them out and restore a very vital society.

**Q:** What will you do to stimulate the economy?

**A:** What I have to do in the next year or so is restore the economy so that competitive manufacturing in-

dustries don't feel they have to leave Japan [but] feel more secure to do business [here at home]. I will use any weapon in my power, whether it's tax policy or anything else. In five years' time, we would like to base our economy on new scientific and technological development. Maybe government will have to make aggressive investment in research and development where we've solely depended on the private sector.

**Q:** Would you use public money to bail out the banks?

**A:** If we find out that [private] resources are not enough, then I would like to use some public money.

**Q:** Recent policy moves have cooled off the yen. Will moves to deregulate the economy follow?

**A:** Deregulation has been accelerated in many areas. In the past year, we have seen deregulation in the gas and electric businesses. There is a lot more to do. We have to review the existing regulations regarding telecommunications.

**Q:** Your tough performance during the U.S.-Japanese auto talks suggests you are an economic nationalist. Is this true?

**A:** In most other cases, I have been more cooperative with the Americans. Last year, I was in Washington urging dialogue. If the U.S. side had listened to our suggestions, then we wouldn't have needed to expend unnecessary energy.

**Q:** Japan has protested Beijing's current nuclear weapons testing. Do you view China as a threat in Asia?

**A:** Our position is to abolish nuclear arms. We are against nuclear testing by any country. The biggest issue for Japan is

how we can support China's current position of opening up the country and how we can make that policy stable. We have to appeal to China to act in line with international rules, such as [those of] intellectual property rights.

**Q:** Are the U.S. and Japan destined to be economic rivals?

**A:** Japan and the U.S. should be able to become better partners. Today there is basically no communication in areas other than the economy. When we look back at the postwar era, there was a lot of communication. Now, when Japanese go to the States, all they think about is what to buy. And in the *endaka* era, fewer U.S. tourists come to Japan.

### MODERN SAMURAI

“What I have to do in the next year...is restore the economy so that competitive manufacturing industries don't feel they have to leave Japan”

— RYUTARO HASHIMOTO



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## SOUTH KOREA

### NOW DETROIT'S HEAVY ARTILLERY IS TRAINED ON SEOUL

A closed market has the Big Three pressing for sanctions

**N**ow that a truce has been declared in the U.S. fight to crack Japan's auto market, Detroit's Big Three carmakers have found a new battleground: South Korea, the world's fastest-growing car market and one of the most closed. They're urging the Clinton Administration to get tough if Seoul fails to make concessions in Sept. 19-20 talks in Washington.

The dispute isn't just about wresting a bigger part of the \$17.5 billion Korean market. U.S. policymakers feel bound to challenge other Asian nations copying Tokyo's moves. "Like Japan, Korea is using its sheltered domestic market as an export-launching pad," says one official. "We need to send a message to the rest of Asia that we will not tolerate such unfair competition."

Detroit wants to see the Koreans named in a "Super 301" case, which would trigger sanctions if there is no progress within a year. U.S. Trade Representative Mickey Kantor must decide by Sept. 27 whether to put Korea on a Super 301 priority list.

Korea is miles ahead of Japan when it comes to sheltering home-grown auto makers. Seoul's anti-import manual starts with an 8% tariff and a variety of taxes that boost the sticker price of Ford's \$18,000 Mercury Sable to \$40,000. Add in financing restrictions and an anti-foreign bias periodically whipped up by the government, and it's easy to see why imports accounted for a measly 0.3% of Korea's 1.1 million domestic car sales last year. In contrast, Korea exported nearly 650,000 cars.

**LOW OPINION.** But American officials must be careful. After years of deficits, the U.S. ran a \$1.5 billion trade surplus with Korea in the first six months of 1995, exporting aircraft, high-tech equipment, and grain. A trade fracas would only worsen already-souring Korean sentiment toward the U.S. A U.S. Information Agency poll reports that for

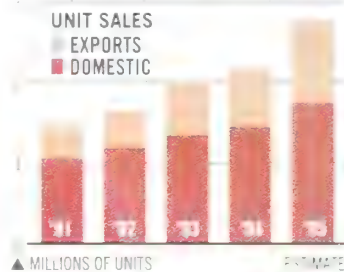
the first time in 12 years, a majority of Koreans have an unfavorable opinion of the U.S.—and 75% cited trade pressure as a main reason for disliking America.

In addition to autos, Korea faces three other possible Super 301 actions. U.S. orange growers are challenging its foreign-citrus licensing system, which shuts



**HYUNDAIS:** Huge profits fund a massive production increase

### KOREAN CARMAKERS ARE DRIVING OVERSEAS



out all but the lowest-grade oranges. California almond growers fume over customs rules that keep shipments on Korean docks for up to eight weeks. Medical device makers are angry about regulations requiring foreign companies to reveal proprietary information.

But Korea's auto policy is the only one likely to make the USTR list. The market has allowed car companies to amass a domestic profits war chest that is funding a huge boost in production. Before the end of the decade, Korea's Daewoo, Hyundai, and Kia will be building 5 million cars and exporting 3 million of them. U.S. auto makers fear Korea will soon be dumping rock-bottom-priced cars in

Asia, Eastern Europe, and Latin America, where they want to compete, too. "Korea can cause a bigger problem in world trade than Japan has," says Ford Motor Co. Chairman and CEO Alexander J. Trotman.

Detroit wants Korea to reduce its import tariff, eliminate taxes on cars with larger engines, junk some safety standards, and speed up liberalization of curbs on foreign participation in auto financing. So far, it is getting rhetorical support from Europe, which opposes America's tough tactics in the U.S.-Japan auto dispute. "The Koreans... cannot keep their markets closed while they go gallivanting around the world," says James Rosenstein, spokesman for

the Association of European Automobile Manufacturers.

Officials in Seoul counter that they are slowly opening up their auto market. Since 1994, Korea has cut its import tariff from 10% to 8% and permitted foreign companies to own up to 49% of consumer auto-financing ventures. Additional steps are being readied, says Chung Seung-II, an official in the International Trade & Industry Ministry.

That may not be enough. "The Koreans always move. The question is: How far?" says one U.S. official. If Seoul falls short, look for Washington to turn up the heat. Polls show confrontational trade tactics are a political winner for President Clinton. His foreign policy mavens advise avoiding flaps with Japan and China. That makes Korea all the more tempting a target.

By Amy Borrus in Washington, with Keith Naughton in Detroit, and Laxmi Nakarmi in Seoul





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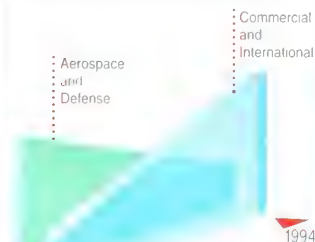
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EDITED BY JOHN PEARSON

## QUEBEC: THE SEPARATISTS SURGE —AND THE MARKETS TREMBLE

One of the world's longest-running suspense dramas—whether Quebec will separate from Canada—is finally headed for a climax. On Sept. 11, the Quebec National Assembly began debating the ruling Parti Québécois' plan to make the French-speaking province a "sovereign country." The debate kicked off an all-out campaign by separatists to win a *oui* vote for sovereignty by Quebec's 5 million voters in an Oct. 30 referendum.

The separatists, led by Quebec Premier Jacques Parizeau, are coming on surprisingly strong. A Sept. 9 survey by Montreal pollster Léger & Léger put support for the *oui* camp at 50.2%. Although most observers still expect Quebecers to tilt in favor of staying within the federal union, "the result will be very tight," predicts CEO Jean-Marc Léger. "The federalists are behind" in organization and momentum, he adds.

**VOTE OUI.** Worries over the outcome are making financial markets nervous. Just weeks ago, the Canadian dollar had risen to an 18-month high amid optimism that Canada would remain united. But the new poll dropped the dollar to U.S. 74.24¢ from its recent peak of 74.93¢. In response, the Bank of Canada on Sept. 12 hiked its lending rate by 35 basis points, to 6.9%. With the risk of recession already a concern, higher interest rates are the last thing Canada's economy needs.

Even a narrow win by the *oui* forces would plunge Canada into the worst constitutional dilemma of its 128-year history. "It would be a nightmare," says Brian I. Neysmith, president of Montreal-based Canadian Bond Rating Service. For starters, Quebec would face an immediate crisis trying to roll over its massive debts, he says. By contrast, a *non* vote would relegate separatism to the back burner for years, although the movement would linger on.

The separatists' unexpected surge is a tribute to the ma-

neuvering of the ever-wily Parizeau. Although he was elected on a platform of hard-line separatism last fall, by the spring it was clear that no more than 40% of Quebecers would vote for a complete break with Canada. So in a skillful shift, Parizeau is asking voters if they agree Quebec should "become sovereign, after having made a formal offer to Canada for a new economic and political partnership." To be sure, Quebec would still write its own laws, claim its own seat at the U.N., and send its own team to the Olympics. But to

avoid economic upheaval, Parizeau in effect proposes to recreate, in a different form, the Canadian confederation he wants to break up. Relations between Quebec and English Canada would be managed by a new superstructure including a joint Parliament.

So far, Parizeau's "partnership" theme has worked brilliantly to win support from "soft nationalists": the 20% of Quebec voters who want autonomy but fear a rough divorce. The hitch is, almost everyone in English Canada thinks Parizeau is peddling an illusion. "The rest of Canada simply doesn't want to deal with Parizeau and his gang," says Vancouver pollster Angus Reid. English Canada would oppose Parizeau's plans to allow Quebecers to use the Canadian passport, he says, and would veto any form of political association. Says Canadian Prime Minister Jean Chrétien, himself

a Quebecer: A *oui* is a "one-way ticket to separation."

Such warnings, the federalists hope, will yet clinch a *non* vote. Most Quebecers, they reason, don't want a nasty breakup of the country, ranked by the U.N. as the world's best place to live. But if Parizeau can convince enough of them that Chrétien & Co. are crying wolf about the perils of a breakup, he could yet pull off a victory. For Canada, and Quebec, it's going to be a nerve-racking fall.

By William C. Symonds in Toronto



PARIZEAU: A wily move

## GLOBAL WRAPUP

### A HAT IN MEXICO'S RING?

► Former Mexico City Mayor Manuel Camacho, one of the country's savviest politicians, is reentering active politics after a year-long silence—and President Ernesto Zedillo's government is uneasy about it. Camacho is believed to be trying to carve out a power base among factions in the ruling Institutional Revolutionary Party (PRI), including moderates who are frustrated by hard-liners' resistance to steps to democratize the party. Camacho's moves could complicate

Zedillo's own attempts to maneuver between reformers and "dinosaurs."

Camacho, 49, a longtime friend of former President Carlos Salinas de Gortari, expected to be the PRI's presidential candidate in 1994. But Salinas tapped Luis Donaldo Colosio. Salinas kept Camacho's career alive by giving him the role of peace negotiator with the Chiapas rebels, but Camacho continued to hint he might make an independent run for the presidency. After Colosio was assassinated and Zedillo took his place as the presidential candidate, Camacho quit as peacemaker

and adopted a low profile. Now he is launching a series of public talks on the need for political change, starting with a speech in Monterrey.

Critics see Camacho as more of an ambitious populist than a reformer. Backers of Zedillo fear Camacho's moves in the PRI could undermine Zedillo's remaining five years in office. Camacho's aim, observers believe, is to step in as the bridge-builder in the PRI after reformers and hard-liners have duked it out—and become the party's standard-bearer in the 2000 election.

By Geri Smith in Mexico City



# DRILL BITS, PAINT HINNER, EYELINER

Sears lures middle-income women with a cosmetics line

Only days after he was named president of apparel at Sears, Roebuck & Co. in February, 1993, Bert L. Mettler was having lunch at New York's posh Ansley Park Lane Hotel with Arthur C. Martinez, president of cosmetics maker Lancôme USA. Mettler, a Montreal native, was talking quickly in his heavy French accent and drawing numbers on a paper napkin. His proposal: that Sears create its own private-label line of cosmetics through a joint venture headed by Martinez, who would resign his position at Lancôme post. Mettler, who was already planning to discontinue the cosmetics business with his new boss, Arthur C. Martinez, then CEO of the Merchants Group, was intrigued. He didn't commit himself, but put the napkin in his pocket. Mettler was born one of the unusual retailing partnerships of the 1990s. Sears linked up with outsiders decades ago to build some of its best brands, such as Kenmore, but never before offered up equity in a brand. The joint venture, signed in April last year, was considered so secret that Sears executives referred to it only by the code name Vincent, a reference to the shaggy creature in the now canceled TV show, *Beauty*



**METTLER AND "VINCENT":** *Their pact was top secret*

and the Beast. After a frantic 17 months of creating, manufacturing, and packaging more than 600 products, Sears unveiled its Circle of Beauty line of makeup, skin-care products, and fragrances in mid-September.

The key question: Will American women, who spend \$16 billion a year on cosmetics and fragrance, buy personal products from a company best known for Weatherbeater paint, Crafts-

man tools, and DieHard batteries? "It's a bit of a stretch," says retail consultant Alan Millstein. There's another obstacle: The cosmetics and fragrance business relies heavily on image advertising, and Sears won't be advertising nationally at first because the cosmetics will be sold in only 150 of its 800 stores.

**SURROGATE SHOPPERS.** Sears, the nation's No. 2 retailer, has a lot riding on the outcome. Cosmetics are the next critical step in its \$40 million-a-year "Softer Side of Sears" marketing campaign, launched in the fall of 1993 to woo middle-income women. Martinez ordered up the campaign soon after joining Sears in 1992, when he discovered that its best customers for its big-selling Craftsman tools and Kenmore appliances weren't men. They were women, aged 25 to 50, who do almost all the family shopping, from buying men's underwear to picking out a new washer.

The bad news: When it came to their own needs, women went elsewhere. Sears didn't carry much brand-name apparel and hadn't built any big in-house brands as it had with tools and paint. The campaign has helped, though those soft lines still represent only about a third of sales because hardware and tool sales have been growing, too. Sears' retailing profits increased 18%, to \$890 million, in 1994. Sales in stores open a year or more jumped 8.3% and are up an additional 4.1% so far this year. But Martinez thinks he can do better.

Sears has spent tens of millions of dollars funding the 50-50 joint venture with Rogers and two associates. It's betting that a market exists somewhere between drugstore blister packs of blush and eye shadow and the high-priced department-store counter. Catherine Wills, Maybelline Inc.'s executive vice-president for marketing, says she's keeping

## Between Class and Mass

*Retail prices for cosmetics*

|                          | Lipstick | Foundation | Blush   | Eye shadow |
|--------------------------|----------|------------|---------|------------|
| <b>DEPARTMENT STORES</b> |          |            |         |            |
| Estée Lauder             | \$15.00  | \$27.50    | \$20.00 | \$10.00    |
| <b>MASS</b>              |          |            |         |            |
| Circle of Beauty         | \$8.50   | \$12.50    | \$10.00 | \$8.00     |
| <b>DISCOUNT STORES</b>   |          |            |         |            |
| Wal-Mart                 | \$8.50   | \$9.25     | \$8.75  | \$7.00     |

**FIRM FOUNDATION:** Sears plans on building its brand slowly



an eye on Circle of Beauty. But she believes the convenience of buying make-up at Wal-Mart Stores Inc. or Walgreen Co. will keep customers loyal.

Sears says its focus-group research found that many chain-store shoppers are intimidated by department stores, where the goods are kept behind glass. But they still want help choosing the right product and color—something most drugstores and discounters don't offer. Sears lets shoppers test Circle of Beauty products themselves while salespeople wait to answer questions. Once they make a choice, shoppers help themselves to the merchandise and carry it to the cash register. "When people can play with products, there's a greater tendency to buy one," says Allan Motus, publisher of the *Informationist*, a cosmetics-industry newsletter.

**EN ESPANOL.** Circle of Beauty's creators took bits of inspiration from current hits. There are botanical ingredients like the Body Shop International's. Skin-care products and makeup are fragrance-free and tested by dermatologists like Clinique's. No animal testing, of course. The packaging, which doesn't mention Sears, is an elegant dark green, not unlike Chanel Inc.'s simple trademark black. But Circle of Beauty costs a lot less. A lipstick runs \$8.50, compared with \$20 for Chanel. And Sears, with a growing number of black and Hispanic customers, offers twice as many shades of lipstick and foundation as most rivals. Brochures are in Spanish and English.

Advertising won't be expensive at first. Circle of Beauty will hit 100 new stores annually, but it will be years before it's sold widely enough to justify national ads. Sears thinks it can afford to move slowly. "We know building a brand is a long-term proposition," says Martinez, who was named Sears chairman in August. "This is not a quick three-month commitment and pull the plug."

If Sears manages to turn Circle of Beauty into a strong contender, the potential is huge. As apparel sales sag, cosmetics and fragrances have come to represent about 10% of department-store sales, up from 6% a decade ago. They carry 40% gross margins, and Sears' profits on Circle of Beauty should be even higher since it's private label.

Sears has done everything it can to make the new line a success. It spent heavily on consumer research, testing everything from names to products to packaging. Beauté, the French word for beauty, for example, was discarded as a possible name because women couldn't pronounce it. Circle of Beauty is certainly easier to say. The question is, will it ever roll as trippingly off the tongue as Kenmore and Craftsman?

By Susan Chandler in New York

## The Corporation

### STRATEGIES

# AT CIRCUS CIRCUS, IT'S BUILD, BUILD

The company is anteing up millions for more rooms

It's show time at the circus—Vegas style. As a high-wire artist warms up above a bleacher filled with popcorn-munching kids, the kids' parents stuff nickels into rows of clanging slot machines nearby. But the star attraction isn't in the next ring; it's two floors above the casino's din. Spread around a wood-paneled boardroom lies the future of Circus Circus Enterprises Inc. There, artists' renderings depict a Venetian-palazzo-style hotel, a cluster of Egyptian-style villas, and a thrill ride set against King Tut's tomb.

It was in that same boardroom a year ago that shareholders forced William G. Bennett, Circus Circus' 70-year-old founder, to quit after months of corporate infighting and slumping profits. Circus—long a Wall Street darling—had lost its luster. From 48 in late 1993, Circus' stock slumped to 20 a year later. "It was a pretty bad time," admits Clyde T. Turner, Bennett's understated successor, "one we intend to put behind us."

**GLORY DAYS.** In Las Vegas, where the only way to win is to wager, that means spending big. A rejuvenated Circus intends to do just that. Over the past year, Circus had to sit on the sidelines while rivals such as Mirage, MGM Grand, and Hilton poured on new rooms. Now, Circus is piling its chips on the table, too. On Aug. 28, the board approved Turner's plans to spend upwards of \$400 million to expand its splashy Vegas showpiece, the pyramid-shaped Luxor Hotel & Casino, with 1,780 new rooms, high-tech rides, and new meeting areas. And as Circus moves into Atlantic City for the first time, Turner will spend as much again: He has joined with Mirage Resorts Inc. in a \$1 billion bid to build two hotel-casinos that won city council approval in early September. In

all, says President Glenn Schaeffer, spending could run into the billions as Circus adds up to four major casino-hotels by 2000.

The building boom marks an effort to return to Circus' glory days. Under Bennett, its formula had long been unique. Eschewing credit and high rollers, Circus



**THE CHIEFS:**

Ensign, Turner, and Schaeffer are ready



**THE SHOWPIECE:** Luxor is expanding

caters to heavy-betting blue-collar gamblers by offering low-priced rooms and cheap buffets. By adding clowns and theme-park-style amusements, Bennett—who had run Circus with an iron fist since 1974—was also the first to make Vegas family entertainment. As a result, cash flow and margins have always topped the industry.

But Circus' luck recently ran cold. Soaring construction costs sent earnings down for the first time in 1993.

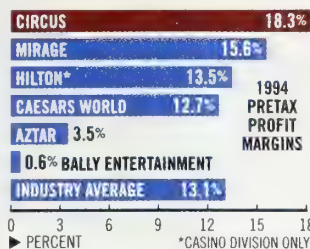


...rivals began making  
...ds into Circus' hold on  
...mass market. Both the  
...Grand and Mirage's  
...sure Island hotel have  
...ed with cheap rooms  
...meals aimed straight  
...Circus' clientele.

...aving opened two new  
...os itself in the past  
...Circus' earnings are  
...vering: Operating in-  
...for the first six  
...hs of 1995 was up 8%,  
...51.9 million, on a 6%

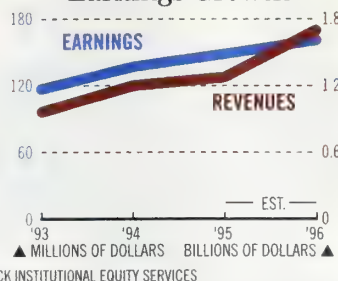
...gain, to \$621.7 million. But most of  
...ains came from Circus' new Tunica  
...boat in Mississippi, and a jointly  
...ed casino in Reno. At its three  
...st casinos—Circus Circus Las Ve-  
...Excalibur, and Luxor—profits have  
...red. The company has also faced  
...internal problems: Unwilling to give  
...ontrol, Bennett had systematically  
...ed a host of potential successors

## Circus Tops Rivals In Profitability...



DATA: COMPANY REPORTS, HANCOCK INSTITUTIONAL EQUITY SERVICES

## ...But Expansion Slows Earnings Growth



it easy for gamblers to ro-  
tate among Circus' proper-  
ties—they figure profits will  
grow as more gamblers  
crowd their casinos. "The  
upside is just amazing,"  
says analyst Dennis I.  
Forst of Hancock Institu-  
tional Equity Services, the  
brokerage arm of insurer  
John Hancock Mutual Life  
Insurance Co.

Still, downside risk  
looms, too: With extensive  
construction under way in

Vegas—and legalized gambling popping  
up everywhere from Connecticut to Col-  
orado—more casinos are fighting over a  
fairly finite number of gamblers. And  
neophytes lured in by flashy amuse-  
ments spend less. Already, such prob-  
lems have dented Circus' recent open-  
ings. The \$92 million Grand Slam  
Canyon water park added alongside Cir-  
cus Circus Las Vegas has been slow to  
catch on, and the company recently took  
a \$31.5 million writedown for a failed  
Louisiana riverboat project. Moreover,  
cost overruns and lower-than-expected  
wagering have made the \$404 million  
Luxor, Circus' most recent major pro-  
ject, less profitable than anticipated.

**"WE'LL PROSPER."** In Atlantic City—  
which until recently was anything but a  
winning bet for casino operators—the  
stakes are equally high. Although the  
city has loosened restrictions on gam-  
bling in hopes of sparking a revival, the  
potential remains unclear. Circus plans  
to build two adjoining hotel-casinos with  
partner Mirage. But while the city is  
hoping that will provide the excitement  
needed to transform what has been a  
day-trip market into a resort destina-  
tion, many in the industry have doubts.

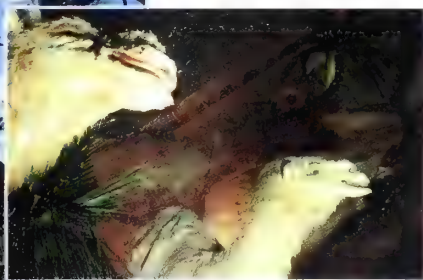
Turner admits that swelling capacity  
will bring a fight. Together with con-  
struction costs, that could hurt profits:  
After years of double-digit gains, ana-  
lysts expect annual growth to slow to  
around 8% (charts). But Turner argues  
it will be the smaller, less glitzy casinos  
that fold. "The big will get bigger," he  
says. "We'll prosper in a shakeout."

With its A-team management back  
in place, rivals also expect Circus to  
avoid its recent errors. "Clyde has self-  
lessly created what is obviously a for-  
midable competitor," says Raymond C.  
Avansino, president of Hilton Hotels  
Corp. And with low debt and the best  
cash flow in the industry, Circus has a  
key ace up its sleeve. "Our cash flow  
gives us the ability to self-finance a lot  
of what we want to build," Schaeffer  
says. If its luck has really turned, Circus  
holds a strong hand to rake in Vegas'  
fiercely contested pot.

By Ronald Grover in Las Vegas

sure to beef up management, Turner paid  
\$500 million for Gold Strike Inn & Casino,  
an operator of small casinos. The real  
lure was its executives. Some 100 of Gold  
Strike's managers had once worked at  
Circus, including Schaeffer and Michael S.  
Ensign, both former heirs-apparent to  
Bennett. Turner installed Ensign as COO  
and Schaeffer as president and CFO. The  
move has reassured jittery sharehold-  
ers—Circus' stock is up  
to 32—and the board. Says Coehlo: "This deal  
gives us the management  
depth that had been sys-  
tematically eliminated  
over the years."

The Circus alumni's first  
chore: finish the 3,024-  
room Monte Carlo casino-  
hotel they're building  
down the Strip from the  
Luxor and Excalibur. The  
\$325 million project, a joint  
venture with Mirage that  
Gold Strike had signed be-  
fore Circus bought it,



**THE GLITZ:** Inside Luxor

the years. By mid-1994, as share-  
holders clamored for change, outside  
members led by ex-congressman  
former Wertheim Schroder & Co.  
aging Director Tony Coehlo pushed  
Bennett out. Bennett, who declined to  
be interviewed, has resigned from the  
board and sold most of his Circus stake.  
The purges left Circus' management  
team painfully thin. Some big sharehold-  
ers questioned whether Turner—the long-  
time chief financial officer at Mirage be-  
fore he joined Circus in 1992—was up  
to the CEO's job. Under heavy board pres-

sure to open next summer. But the key  
to Circus' future lies a mile south of the  
new casino on a 120-acre plot next to the  
Luxor that Turner bought for \$153 million.  
By building up to four new casinos and  
linking the site to the Excalibur and Lux-  
or with monorails and moving sidewalks,  
Turner aims to control a mile-long block on  
the hottest stretch of the Strip.

Turner and his new team hope to  
have nearly 20,000 rooms in Vegas by  
the decade's end—double Circus' size today.  
By building new rooms at a far faster  
clip than new casino space—and making

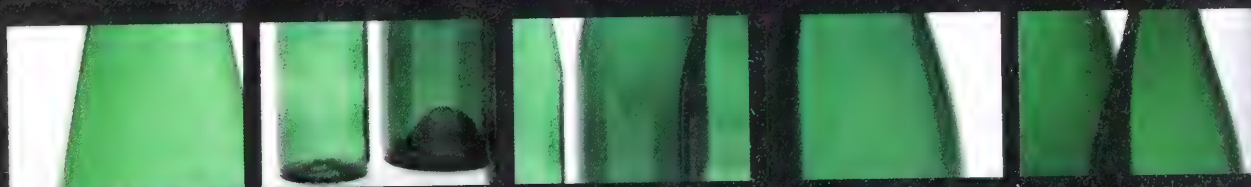




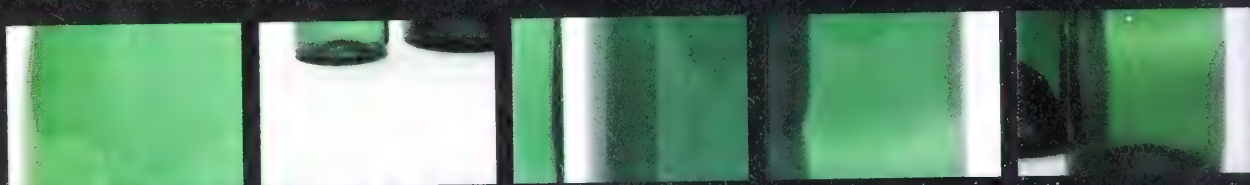
You're on the road. With a client.



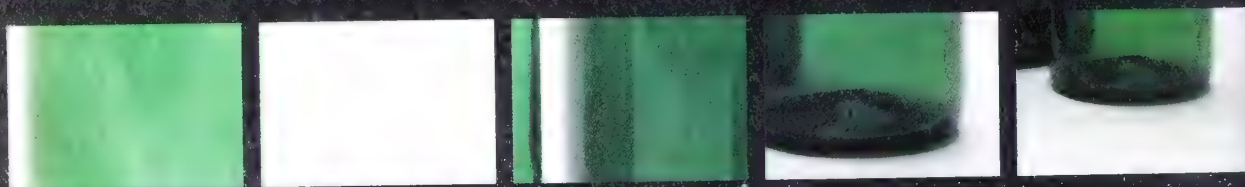
You need to locate a bottle design.



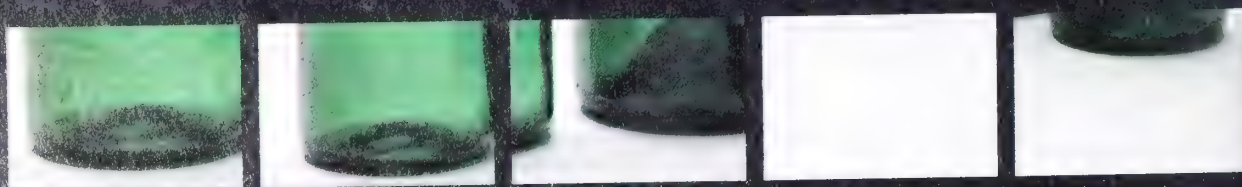
HQ's database has 40,000 bottles.



And all you know is the shape.



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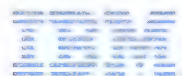
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# Cover Story



PHOTOGRAPH BY TIMOTHY ARFA



# THE PRINCE

## Inside the \$10 billion empire of power player Alwaleed

BY JOHN ROSSANT

It's 2:30 a.m. in Saudi Arabia's desert capital, Riyadh. But sleep is the last thing on the mind of a little-known but impressive young man who is emerging as one of the world's most powerful investors. Sitting in one corner of his new \$20 million futuristic sports complex—complete with tennis courts, high-tech muscle machines, and bowling alleys—Prince Alwaleed bin Abdulaziz Al Saud is working the telephones, canning the globe for new properties. As he talks, a dozen retainers play cards on the floor, while parrots and songbirds warble away in a nearby two-story cage.

It is Alwaleed's performance that rivets attention. In a six-hour blitz, tracking progress of deals, he takes dozens of calls, placed by private operators through satellite uplinks at his palace next door. What's striking is how seamlessly he glides through each conversation, whether it is about financing a hotel in Lebanon or selling a block of shares on the Paris Bourse. Deal-of-the-day is clearly Canary Wharf, the London complex that is Europe's largest real estate project. A call to his new partner, Canadian developer Paul Reichmann, irons out a last-minute snag, meaning a signing will take place within weeks. Alwaleed is confident. "I've got a rule of thumb," he says, "a white-robed servant silently offers small cups of coffee. 'Anything that's worth \$4 billion costs \$1 billion, buy it.'"

That's his appraisal of the deal he and other investors are going on—to take over the huge project on London's River Thames. What he's chipping in is small potatoes for him. His \$10 million investment—10% of a consortium led by the Laurence A. Tisch-controlled CNA Financial Corp.—is less than 1% of his net worth of around \$10 billion (chart, page 92). But this foray illustrates the disciplined, value-oriented strategy that has already propelled this grandson of Saudi Arabia's founder into the investment big leagues.

Alwaleed is probably the most important financial kingpin that you've never heard of. Unlike a George Soros or Rupert Murdoch, publicity-shy Alwaleed mostly stays out of the limelight, preferring to work by telephone from his Riyadh office. But he has already made his mark on several premier deals of the 1990s. Alwaleed's 1991 debut on the world stage was in true grand style: \$800 million to shore up Citicorp, making the Saudi prince its largest shareholder.

Since then, Alwaleed has been building an international portfolio of high-profile but undervalued assets—like a Warren Buffett on a global prowl. He has bought up chunks of Euro Disney, Saks Fifth Avenue, and the Four Seasons-Regent hotel group, the world's largest luxury chain. Last July, the prince made waves in Europe when an Alwaleed-led alliance bested Rupert Murdoch in bidding for a \$1.2 billion stake in the Italian TV empire of media tycoon-turned-politician Silvio Berlusconi.

That move signaled a new direction for the prince. Now, he may become a player in the frenzied buying and selling of media properties. Recently, Ted Turner sounded him out—unsuccessfully—about helping finance a bid for CBS. "We're going to go for a big one," predicts Alwaleed. "With Murdoch attacking from the north, we're going to counter from the south." Offers to come in on other media megadeals routinely cross his desk.

The prince has taken advantage of Saudi Arabia's sudden wealth—and its less-than-sophisticated business environment—to make himself the kingdom's most powerful mogul.

With a bank, a supermarket chain, vast real estate holdings, and a broadcasting operation, his reach in Saudi Arabia is unmatched. Throw in an operation that doles out \$150 million a year to down-and-out Saudis and even needy princes, and Alwaleed is making himself a household name in the kingdom. Could a foray into Saudi politics be his next step—as it was for Italy's Berlusconi, whom Alwaleed admires? Alwaleed dismisses that: "I like being a free man and talking openly. Who wants to be handcuffed?" he says.

Right now, Alwaleed is more concerned with proving that he is very different from the glitzy sheikhs who squandered their

### BUFFETT OF ARABIA

Value investor Alwaleed is much more like the Sage of Omaha than the glitzy petro-sheikhs of the '70s and '80s—and it shows in his portfolio of high-profile assets

WINNING A SPEEDBOAT  
ANNES: HIS 283-  
FT YACHT (FORMERLY  
ALD TRUMP'S) IS  
LONGER CRUISES





petrodollars so fast in the 1970s and 1980s. Many of these would-be global tycoons turned out to be the world's biggest suckers instead. Some of Alwaleed's royal relations got lured into the Hunt brothers' bungled scheme to corner the world silver market in the 1970s. More recently, Abu Dhabi's ruler, Sheikh Zayed, was fleeced of billions of dollars by the scandal-ridden Bank of Credit & Commerce International. With his studied approach, Alwaleed is as different from those high rollers as Buffett is from Donald Trump, whose 283-foot yacht the prince bought at the knockdown price of \$18 million from Trump's creditors in 1991. Even though not all of his investments have been home runs, the prince has an enviable track record. In the past 12 months alone, the prince has ratcheted up over \$2 billion in paper profits on his Citicorp and Euro Disney holdings. And, as Alwaleed might himself remind you, at age 38 and with \$10 billion in his pocket, this fitness fanatic, who doesn't drink or smoke, is just getting started.

Along with other big investors, Alwaleed and his small band of advisers get first crack at some of the biggest deals going. When Kirk Kerkorian went after Chrysler Corp. recently, the tycoon offered

## Cover Story

Alwaleed a stake. It was turned down flat. "Kerkorian was using me for leverage. And anyway, buying in at \$56 in hopes Chrysler would go to \$100 wasn't interesting enough," says the prince. "When it comes to deals outside Saudi Arabia, I don't go against management." Also receiving thumbs down recently: stakes in Britain's Saatchi & Saatchi and a global satellite telecommunications system.

In fact, perched behind Alwaleed's huge desk at his Riyadh headquarters is a three-foot-high pile of confidential prospectuses from Lehman Brothers, Merrill Lynch, Goldman Sachs, and Alwaleed's own consultants around the world. Looking at the printout of his global holdings, which aides prepare for him each week, he says he aims "to go to \$15 billion [in assets] in three or four years."

Don't expect impetuous moves. Although his key aides

## DESERT COMMAND

Satellite links keep the prince in touch with his global holdings—as he stays in touch with his Bedouin roots

is a workaholic. When he takes his regular late-night jog through the deserted streets of Riyadh, aides run behind him carrying constantly ringing cellular phones. And Alwaleed takes one vacation each year—a three-week stay on his yacht in the French Riviera—is crammed with meetings with potential partners. This last August, for example, Alwaleed sent his plane to fetch pop star Michael Jackson for an onboard lunch and a discussion of a joint marketing operation. Days later, Monaco's Prince Albert was feted—to help swing approval for a new, multimillion-dollar Four Seasons hotel in Monte Carlo.

**FIFTY SLAVES.** How did this son of Arabia climb to such a lofty position so fast? Many have assumed the slim, 5-foot-8-inch, 140-pound Alwaleed is a one-man investment front for other, more publicity-shy Saudi princes. Some have whispered about contracts to build secret military bases in Saudi Arabia—even fat commissions on oil shipments. Alwaleed himself has done much to quell the rumors. The prince has put out an implausible story about starting out with a modest \$35,000 from his father. Now, through dozens of interviews with the prince and associates, BUSINESS WEEK has pieced together the tale of how this determined investor built up his empire.

Of course, Alwaleed was never poor. But when the prince was born in 1957, Riyadh was still a forbidding desert town largely closed to foreigners. But, as the son of Prince Talal, the 21st son of Saudi Arabia's first king, Alwaleed enjoys

number less than 10, potential deals are rigorously studied. Arthur Andersen & Co. is kept on retainer to evaluate every new investment lead, such as Hogan & Hartson, a tony Washington (D.C.) law firm. Citibank also chimes in, from sizing up new projects to daily air shipments of U.S. and British newspapers for the prince to scan. In spite of the glittering trappings of Alwaleed's great wealth—his yacht, a Boeing 727, and a fleet of 250 cars and motorized caravans—the prince



privileges unknown to most Saudis: running water, cars, and a radio that his father toyed with as a hobby. Until his father freed them when Alwaleed was 5, some 50 slaves were needed to keep order at home.

But the kingdom's wealth was nothing like it is today. Oil, which American companies were pumping some 350 miles eastward, fetched just pennies a barrel on world markets—and the Saudi government was in a constant financial bind. In fact, King Saud, whom Alwaleed's father briefly served as Finance Minister, was deposed by his brother Abdul Aziz in 1964, in part because his spendthrift ways threatened to throw the kingdom into bankruptcy.

What all changed in a flash. The oil-price explosion of the 1970s brought fabulous wealth, and the Al Saud clan—which numbers around 6,000 princes—became collectively the richest and certainly the largest royal family on earth. The Al Saud maintain a tight grip on Arabia, as they have since Alwaleed's grandfather, the formidable Abdulaziz, unified most of the vast Arabian peninsula in the 1920s. Today, Alwaleed's uncles, sons of the founder, fill the top roles in the kingdom: King, Crown Prince, Ministers of Defense and Interior. For nothing has Saudi Arabia been called "the only family business with a seat at the U.N."

But Alwaleed is an Al Saud with a difference: In 1962, his father and four of his brothers revolted against the rest of the family. Talal showed sympathy for an Al Saud enemy, Egyptian revolutionary Gamal Abdel Nasser, and publicly called for a more open political system. This affair was a serious, embarrassing rift within the family and led to exile for Alwaleed in Egypt, where he was exploited by Nasser's propaganda. He was eventually allowed to come home. Ever since, an unspoken rule among the Al Saud has been that no son of the late King Talal—and, by extension, his family—from an "illegitimate" role in government. Alwaleed was free to make money," says a former U.S. ambassador to Saudi Arabia. "But he was never really forgiven."

**THE TRANSCRIPT.** This is the one subject

that normally loquacious Alwaleed will not dwell on. But being something of an outsider goes far to explain his drive to succeed in business. From the age of 16, he says, "I realized I wanted a car and a boat and to make money." That was easy for Alwaleed at the top of the Saudi hierarchy—sons of the King and full brothers—but more difficult for others.

As a grandson of Abdulaziz, Alwaleed gets a monthly \$100,000 check from the royal court. With close to 400 people on his private payroll—ranging from the 160 employed at his Riyadh palace to his yacht's 40-man crew and the two gunning guards who follow him 24 hours a day—that stipend covers less than 2% of his household expenses. This is the lifestyle expected of a senior prince, not a minor royal.

Early on, this outsider prince says he saw himself on a mission—to make his mark through business. That was evident when Alwaleed landed in San Francisco in 1976 to begin undergraduate studies in business at Menlo College. Unlike any other rich Saudis who went to Menlo, Alwaleed applied himself with a concentration that is remembered even today. "He was the hardest worker I have ever seen," recalls Carlos U. Lopez, Alwaleed's academic adviser.

After Alwaleed's first year, an anxious Talal dispatched an emissary to California to find out whether his son was study-

## A Fast Rise From Not-So-Humble Beginnings

**1957** Born in Riyadh to Prince Talal bin Abdul Aziz and Mona al-Solh, the daughter of Lebanon's first Prime Minister

**1960-8** Lives in Beirut with his mother after parents' divorce

**1962** His father, Prince Talal, attacks the Saudi system, goes into exile

**1979** Gets honors degree in business from Menlo College in California

**1980** Sets up Kingdom Establishment, the foundation of his empire



**IN UNIFORM AT 14:** He still leads a life of discipline

**1982** Wins the first of his many lucrative Saudi military construction contracts, representing a South Korean builder

**1986** Shakes the Saudi business world by taking over troubled United Saudi Commercial Bank

**1991** Comes to the rescue of Citicorp, his biggest deal

**1994** Bails out shaky Euro Disney theme park

**1995** Buys 50% of New York's Plaza Hotel for \$160 million

**1995** Negotiates for 10% of London's Canary Wharf with developer Paul Reichmann and others



**ON BOARD:** Alwaleed and Reichmann have hit it off well



**ALL WRAPPED UP:** Alwaleed is by far the largest shareholder of Chairman John Reed's Citibank



ing enough. "He said Alwaleed's father was worried that his son might not be doing well," remembers Lopez. "I said: 'My God, have you seen his grades?' They were straight As." A framed copy of Alwaleed's transcript from Menlo hangs on the wall of his palace today.

But Alwaleed acquired his financial skills on the job, not from textbooks. When the prince returned to Riyadh in late 1979, it was an auspicious moment to start out in business. Oil prices were breaking records, and the government was pumping billions of dollars into construction, from superhighways and new ministries to squadrons of the fanciest fighter planes ever built. It was a gold rush that transformed the kingdom and made overnight millionaires out of many Saudis. Under Saudi law, every foreign company with work in the kingdom must have a local sponsor—who pockets around 5% of any contract.

In 1982, after setting up a company called Kingdom Establishment in a tiny prefabricated office, Alwaleed landed his first deal: an \$8 million job to build a bachelors' club at a military academy near Riyadh. He was representing a small South Korean contractor.

From then on, the prince's business grew rapidly and became more sophisticated. Instead of acting as mere agent, Alwaleed boosted his profits by setting up his own companies to form joint ventures with foreigners. With that, Alwaleed

## The Prince's Empire

| HOLDING                       | % SHARE | COST (MILLIONS) | CURRENT MARKET VALUE (MILLIONS) |
|-------------------------------|---------|-----------------|---------------------------------|
| <b>NORTH AMERICA</b>          |         |                 |                                 |
| CITICORP                      | 9.9%    | \$590           | \$2,800                         |
| FAIRMONT                      | 50      | 40              | \$100                           |
| PLAZA HOTEL                   | 50      | 160             | NA                              |
| FOUR SEASONS HOTELS           | 26.6    | 124             | 97                              |
| SAKS FIFTH AVENUE             | 11      | 100             | 200                             |
| <b>EUROPE</b>                 |         |                 |                                 |
| EURO DISNEY                   | 24.8%   | \$350           | \$600                           |
| CANARY WHARF (pending)        | 10      | 100             | NA                              |
| FININVEST (ITALY)             | 5       | 230             | NA                              |
| BALLAST NEDAM                 | 7       | 50              | 50                              |
| <b>SAUDI ARABIA</b>           |         |                 |                                 |
| UNITED SAUDI COMMERCIAL BANK  | 40%     | \$90            | \$350                           |
| AL-AZIZIYA PANDA SUPERMARKETS | 78      | 140             | 300                             |
| ARAB MEDIA                    | 30      | 90              | 90                              |
| NATIONAL INDUSTRIALIZATION    | 40      | 100             | 100                             |
| SAUDI STOCKS                  |         |                 | 1,500                           |
| RIYADH REAL ESTATE            |         |                 | 2,000                           |
| CASH                          |         |                 | 1,000                           |
| AIRPLANES, YACHT, HOUSES      |         |                 | 180                             |

DATA: BUSINESS WEEK, KINGDOM ESTABLISHMENT

## Cover Story

princes and rich Saudis, who represented companies and just sat back," says Amr Khashoggi, CEO of Saudi Arabia's largest cement maker.

Alwaleed used this new stream of cash to play for high stakes in the white-hot Riyadh property market. Alwaleed's portfolio of 25 million square feet of prime Riyadh real estate and 14 square miles of property just outside the city makes him the largest private landowner in the Saudi capital today. The value: "at least \$2 billion," says Alwaleed.

For a property owner with a sharp eye, Saudi Arabia's poorly managed banks were a ripe target. In 1986, the Saudi establishment woke up to its first hostile takeover when Al-

waleed announced he had secretly amassed a controlling stake in the loss-making United Saudi Commercial Bank. Appointing a new board and management, Alwaleed cut the bank's staff from 600 to 250. And in a country where imported labor is often treated poorly and stock options are unknown—Alwaleed quickly instituted twice-yearly employee meetings, where he hands out cash and keys to new cars to top performers.

The formula worked. USCB was back in the black by 1988 and was Saudi Arabia's most profitable commercial bank by 1990. The bank also provided a gold mine of business intelligence. As USCB chairman, says Alwaleed, "I got to know very well the strengths and weaknesses of local companies." Alwaleed's Kingdom now has majority stakes in companies ranging from Saudi Arabia's largest supermarket chain to fast food, livestock, and hospital management. With \$1.5 billion in the form of minority stakes in large Saudi companies, Alwaleed is set to become even bigger.

Too big, maybe? The balance between royals and commoners in Saudi Arabia's business world is already an uneasy one, with many griping over senior princes' easy access to rich deals. Tempers flared recently when Al-Mawarid, a Riyadh conglomerate controlled by two Al Saud princes, strong-armed several local businessmen into handing over dealerships. Alwaleed claims he'll be immune to criticism: "People know that when I take over a company, I fix it up, and it will be in safe hands. I'm Saudi. I'm dedicated to the nation, and I'm involved in charity."

Although Alwaleed says he gives out of Islam's admonition to help those less fortunate, it's also a way of buying popularity and protection on a massive scale. Using a bank of Compaq personal computers, two full-time Muslim scholars direct a staff of 20 as they dole out one-time cash grants of \$800 to \$2,000 for up to 6,000 needy Saudis a month. His handouts to Bedouin tribesmen visiting Alwaleed's camps are talked about across the country—as was his publicized gift of \$8 million in July to help Bosnian Muslims. But all this is not kept him from being blasted by a London-based Saudi opposition group.

It is not surprising that Alwaleed would want to extend his reach outside Saudi Arabia, if only to diversify his holdings. Long before he made his first big move, he began working

# Alwaleed spreads the wealth, supporting needy princes and doling out cash to up to 6,000 poor Saudis a month

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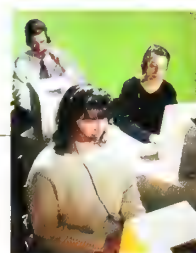
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## WITH SON, KHALED

Sumptuous daily meals are held at odd hours to accommodate a prince whose cellular phones ring into the night

for a capital injection of \$590 million.

"I was the only one in the world willing to talk to Citi," Alwaleed claims today. Was he contacted by the Federal Reserve as part of Citi bailout, as some have suggested? The prince says that's nonsense. "The only time we had contact with the

his global bargain-hunting game plan. "I got a call from Alwaleed in late 1987 asking me to collect as much information as possible about U.S. money-center banks," recalls one of Alwaleed's Swiss private bankers. "He thinks of moves three or four years ahead."

## Cover Story

At the time, Citicorp was just one of several possible targets. By 1989, Alwaleed was snapping up shares of Citicorp, Chase Manhattan, Manufacturers Hanover, and Chemical, sometimes calling in buy orders from a cellular phone while horseback riding in the desert. Within months, he had spent close to \$250 million—at one point holding a 2.3% stake in Chase. "But then, I sold everything and concentrated on Citibank," remembers Alwaleed.

He says he decided that Chemical and Chase were too concentrated in New York and lacked the global brand presence of Citi. On the surface, it was a strange choice: Among the four banks, it was clearly the worst performer, because of a combination of New York real estate loans and exposure to Third World debt. In fact, by late 1990 it was widely feared that the bank might fail.

The crucial moment came in 1991, as the U.S. and its allies were on the verge of ousting the Iraqis from Kuwait. Since Alwaleed, as a Saudi prince, was duty bound to remain in the capital during the Gulf war, lengthy bull sessions on the Citi stake with his lawyers, Al Christianson and Mark Mezou, were interrupted several times by Iraqi attacks. Having already bought 4.9% of Citi's common stock at an average price of around \$12, Alwaleed and Citi worked out a special convertible preferred issue in return

Fed was when we were going over 9% and needed the approval."

The deal put a floor under Citi, and it has also turned out very well for Alwaleed: His 9.9% stake is convertible at just under \$16 a share. With the bank in better shape and Citi common stock selling in mid-September at a 15-year high of \$78, Alwaleed's stake has more than quadrupled in value, to \$8 billion.

What does Alwaleed think of Citi now? If Chairman and CEO John Reed continues to cut costs, says the prince, Citi shares will continue their ascent, to \$100 in the next two years. Returning a call from Citibank Vice-Chairman Paul Collins, Alwaleed gently admonishes the executive to move more quickly on paring overhead. Being a mere shareholder, he knows Reed and Collins needn't take his advice: "But I didn't trust them, I wouldn't put my money there," he says.

Although Alwaleed has been one of Citi's most important private clients since he started in business 15 years ago and took out a \$300,000 loan, using his Riyadh palace as collateral, the prince had never met Reed before directly investing in the bank. That's changed. Now

the two have a long discussion at least once a year, most recently just hours after the mid-August announcement of the Chase-Chemical merger. In 1993, Reed and his son flew to Saudi Arabia and donned Bedouin robes for a late-night party at Alwaleed's high-tech camp 10 miles from Riyadh—complete with roast camels, Bedouin dancers, and some target practice with machine guns.

If Alwaleed is merely a passive—if important—investor in Citi, he's taking a more hands-on approach to hotels. "It's natural for him," says Chuck Henry, an ex-director of real

## Scion of a Desert Kingdom

### THE PRINCE'S FAMILY TREE

**ABDULAZIZ BIN ABDUL RAHMAN ALSAUD 1880-1953**

Founder of modern Saudi Arabia. Fathered 45 sons including:

**SAUD 1902-1969**

King from 1953 to 1964, when he was deposed by his brother Feisal.

**FEISAL 1904-1975**

King from 1964 to 1975, when he was assassinated by a nephew.

**KHALED 1912-1982**

Succeeded Feisal.

**FAHD 1921-**

Present King.



**TALAL 1931-**

Finance Minister under Saud. Rebelled and went into exile in 1962. Later returned. Businessman, roving ambassador for UNICEF.

**PRINCE ALWALEED 1957-**

Saudi Arabia's top businessman. Son, Khaled, 16. Daughter, Reem, 13.



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# "Reichmann is an Orthodox Jew, and I'm an orthodox Muslim. We're both orthodox, so where's the problem?"

estate investments at CS First Boston, who now serves as Alwaleed's full-time hotel-industry consultant in New York.

Alwaleed owns big stakes in New York's Plaza Hotel and San Francisco's Fairmont chain, but the centerpiece of this strategy is the holding he bought in Toronto's Four Seasons Hotels Inc. The price he paid for 26.6% of Four Seasons, \$124

million, stunned the hotel industry.

Although the investment's value

## Cover Story

has fallen, Alwaleed is now busy laying plans with Sharp to expand the 40-hotel group to 60 properties within five years and 80 within a decade. Alwaleed doesn't bother to attend board meetings, but he and Sharp are regular phone pals. Sharp admits he approached their first meeting—on the prince's yacht—with some apprehension: Before the two got down to talking about a potential deal, Sharp says, "I made it clear that I am Jewish and that I have significant ties to Israel. If that's a problem, we shouldn't even get started." Alwaleed immediately assured Sharp there was no problem.

Indeed, many of Alwaleed's closest partners are Jewish, from Sharp and Walt Disney CEO Michael D. Eisner to property czar Reichmann. Sometimes this leads to bruised feelings. Following Alwaleed's big move into Euro Disney in 1994, Eisner was stung by newspaper stories saying that he would not be able to visit Saudi Arabia because of his religion. He sent Alwaleed an angry fax. Alwaleed now says he has an open invitation. After Reichmann plotted business deals on Alwaleed's yacht last August, the prince says he was taken aback when an aide inquired if the Canadian's deep religious beliefs were an obstacle to working together. Alwaleed joked: "I told him: 'Reichmann's an Orthodox Jew, and I'm an orthodox Muslim. We're both orthodox, so where's the problem?'"

"He is traditional and religious, yet modern," Reichmann says. "From others who have dealt with him, I know that when a transaction is completed, it conforms 100% to the initial formulation."

The prince's biggest deal after Citi was his buy into Euro Disney, the \$4 billion park near Paris. With \$3 billion in debt, the park opened in 1992, just as recession set in. After looking at the numbers, Alwaleed was convinced the problems weren't permanent. Says the prince: "It wasn't that people hated Paris, or the weather, or Disney. The problem was simple overleveraging. They just didn't have enough to cover the debt."

Alwaleed and his top adviser, Riyadh businessman Mustafa Al-Hejeilan, say the buyout of a 24% stake June, 1994, was the most difficult and complicated deal yet. After 16 days of negotiations in Paris, Alwaleed squeezed the banks into forgoing interest payments until 1997—worth as much as \$500 million. He also forced Walt Disney Co., which has a 39% stake in Euro Disney, to say *au revoir* to \$70 million a year in management and royalty payments until 1999.

Even with that, many scoffed at Alwaleed's wisdom in investing in the loss-making park. But with attendance up sharply and the company turning its first profit in the June quarter, Alwaleed's \$300 million has doubled in value.

The big hit at Euro Disney could, however, be a trap for Alwaleed. Like many an industrial baron before him, the prince seems to have an itch to get involved in media and showbiz—fields that have already proved treacherous for outsiders.

Over the past two years, the prince and another Saudi coon, Salah Kamel, have pumped more than \$300 million into launching a five-station chain, Arab Television & Radio (ARTV). The somewhat starstruck Alwaleed personally runs ARTV's music channel and seems to relish hobnobbing with the top singers of the Arab world.

Alwaleed says his media operations and his foothold in European TV are the stepping stones to something much bigger. The prince hints he's tempted to enter the frantic bidding wars changing the face of U.S. broadcasting—but first prices are high. But there's another aspect, one that explains why Alwaleed has avoided any hostile takeovers in the U.S. "I don't need people saying the damned Arabs are taking over." If he moves in media, he says, it will be with such partners as Italy's Berlusconi and Germany's Leo Kirch.

## ACTION JACKSON

"We want to create a new multimedia empire. The prince is sweet ... and wants to do incredible things. Just like I do"



The prince's Hollywood bent has led to a budding relationship with recording star Michael Jackson. Last December, Alwaleed and Jackson MJJ Productions signed a confidential agreement to set up a joint company to develop movies, animation, resorts—everything but song recording. Gushes Jackson: "We want to create a new multimedia empire. The prince is sweet and humble but at the same time very daring and wants to do incredible things. Just like I do."

It sounds a little too ethereal, but with Alwaleed's track record, who can say he won't turn whatever he touches into gold? In the guest book on Alwaleed's yacht, in between flowery thank-yous from scores of guests, one message from a top Citibank executive stands out. "I've worked with Your Highness for 15 years," he writes. "Now, I look forward to the next 15 years, when you will become the most powerful and influential businessman on earth." Obsequious? Certainly. But he's probably not way off the mark.

With William C. Symonds in Toronto, Stanley Reed in New York, and bureau reports



# 'IF THERE'S ANYTHING I HATE, IT'S FAT'

Alwaleed bin Talal may relish the role of the modern, global business executive who hashes out late-night, multimillion-dollar deals with such luminaries as Chairman Michael D. Eisner of Walt Disney Co. But above all, he's a prince of the royal house of Saud. I see just how much this means the moment he touch down at Riyadh airport in his private beige-and-green Boeing 727. The plane taxis to a corner of

sink in his own barber shop to the private apartments of his 16-year-old son, Khaled. Outside the palace is parked the boy's \$250,000 Lamborghini Diablo. "I try not spoil them, but I can't deny them things, either," says Alwaleed, speaking of Khaled and his 13-year-old sister, Princess Reem. Both affect an unprincely grunge look outside of the kingdom. Alwaleed and his wife, Princess Dalal, divorced 10 months ago.

col at the table set for 20. Several of Alwaleed's Bedouin retainers—some 60 trusted men, many of whom have spent their lives in the employ of Alwaleed or his father—joke with the prince as they tuck into their food. He clearly loves this sort of familiar repartee, even though he can't resist breaking away to do business on the telephone beside his place.

This strange mixture of informality, royal deference, and what Alwaleed calls his "workaholism" is present when he takes the steering wheel of his Mercedes-Benz S600 V12 for a spin around town. I still haven't figured out how he manages to drive the car and carry on two separate telephone conversations all at the same time. "Would you just look at that land? I love it," he says, pointing to a huge lot downtown that cost him more than \$200 million when he picked it up some years ago. It's where he plans to put up a Four Seasons Hotel, which he says will be the most luxurious hostelry in the Middle East, together with a shopping center that will include the first-ever overseas branch of Saks Fifth Avenue, the department store of which he is a major shareholder.

Being a prince is clearly a full-time job. When he returns to the palace at 3:15 a.m., after a one-hour jog, 60 or so impoverished Saudis, half of them veiled women, are waiting outside. Retainers herd them into his presence

in the courtyard. An aide hands each one a crisp, 1,000-riyal bill—around \$300. Drinking a glass of cool water, the prince silently acknowledges yells of "May you live in paradise," as the beggars are led back to the street. A prince's work, it seems, is never done.

*By John Rossant in Riyadh*



the tarmac, where a fleet of shiny black limousines is waiting, alongside dozens of family retainers. When Prince Alwaleed descends from the plane, each one of them comes forward and kisses the prince's right shoulder—a traditional Bedouin sign of respect. Then, the motorcade speeds off into the Arabian night: There is no passport check, no lost luggage, no waiting around for a lift.

**300 CALORIES A DAY.** Back at Alwaleed's palace in northern Riyadh, where other Al Saud princes live in a kind of royal ghetto, I discover a world that only the combination of almost unimaginable wealth and royalty can produce. He seems proud of the sheer scale and quantity of everything, from the high-tech video systems and the gold-plated taps on the

Lunch, served each day around 5 p.m.—to accommodate a man who regularly goes to bed at 4 a.m.—is unbelievably lavish. But an abstemious Alwaleed just picks at the dozens of delicacies, including baked pigeons and baby camels. He's on a strict, 1,300-calorie-a-day diet designed by his private doctor. "If there's one thing I hate, it's fat," says the prince, who is trim and athletic and also somewhat vain. He keeps himself fit by whacking tennis balls around with Romeo Rafon, a top-seeded ace from the Philippines who is now employed at the palace in Riyadh.

There's little in the way of proto-

## HIGHFLIER

Alwaleed logs 700-plus hours a year in his Boeing 727. The revamped plane seats 34—in comfort



# SOROS: ANATOMY OF A COMEBACK

After a dismal year, the hedge fund guru reveals how he has regained his momentum



## QUICKSAND

“I was concerned... that we were actually sinking”

—GEORGE SOROS

**G**eorge Soros has faced down many adversaries in his 65 years. Nazis in his native Hungary. Communist dictators suspicious of his philanthropy and advocacy of open societies, and, more recently, the central banks of Europe. Soros gained fame a couple of years ago as “the man who moves markets,” by aggressively trading in currencies and bonds. As a trader and investor, his long-term record is unsurpassed—an average annual return of 35% since 1969, among the best in the world. But in recent months, it seemed, Soros was facing a threat as daunting as any posed in the past. His flagship \$6.1 billion Quantum fund was struggling. Its reputation was in jeopardy.

The tension at Soros’ headquarters, across the street from New York’s Carnegie Hall, was almost palpable. In the first three weeks of 1995, Quantum was down 6%, and it fought to break even unsuccessfully through mid-February. In the past, such declines were just temporary setbacks after good years, such as Quantum’s

21,000

20,000

19,000

18,000

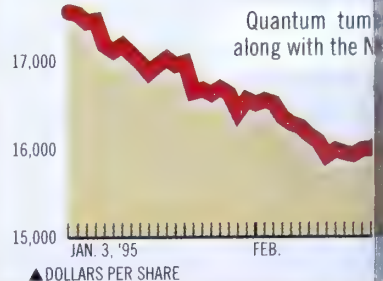
17,000

16,000

15,000

## A QUANTUM LEAP FOR SOROS FLAGSHIP FUND

QUANTUM FUND NET ASSET VALUE





from 1990 through  
Soros was trou-  
"I was concerned,"  
oted the other day,  
it was not a soft  
ng—that we were  
lly sinking."  
was as if the mar-  
were conspiring to  
oy him. Soros and  
chief lieutenant Stan-  
Druckenmiller bet  
e dollar as 1995 be-  
—and it fell. They  
on the Japanese  
et—and it fell.  
e exposure to the  
stock market  
ed inadequate, and

## CHANGING COURSE

“Our worldwide fixed-income gains this year are larger than our currency gains”

—STANLEY  
DRUCKENMILLER



was where the action was. Driven  
financial stocks and a boom in tech-  
y, the S&P was up 20% at the end  
e first half. Quantum was down  
July began hot and sticky in the  
End of Long Island, where Soros  
t most of the summer. But then  
the shower of green.

**MAJOR PICKS.** During the first two  
s of July alone, the Soros-Druck-  
er team moved their humongous  
olio skyward 9%—a half-billion-  
gain worthy of the Soros of yore.  
, in August, Quantum began a  
ly climb, gaining 17% in that  
h alone (chart). During the same  
d, the S&P sputtered and profit-  
g dogged the high-tech stocks.  
ember began as spectacularly as  
e glory days, with a \$100 million  
t gain on Sept. 5. On Sept. 13,  
tum reaped a heady \$200 million  
fall, largely through a leveraged  
on the dollar. Through Sept. 13,  
tum is up 24% after expenses and  
vs. 26% for the S&P.

How did Soros and Druckenmiller  
pull it off? Soros has been mum—until  
now. In separate interviews with  
BUSINESS WEEK, a tanned and cheerful  
Soros, and his dour chief lieutenant  
Druckenmiller, disclosed for the first  
time how they managed to achieve this  
stunning reversal. Yes, currency trad-  
ing played a role in Quantum's reviv-  
al—but a far more limited role than  
has been rumored. Stock selection, he  
and Druckenmiller insist, was a major  
factor in Quantum's recovery.

Soros even disclosed the fund's larg-  
est stock holdings—a nearly unprece-  
dented step for Quantum, except for  
its rarely publicized annual reports.  
But even while de-emphasizing the role  
of macro trading, he made it clear that  
he will increase his use of leverage as  
Quantum's fortunes improve. Clearly,  
he already has—as the Sept. 13 surge  
indicates. Druckenmiller acknowledges  
that he is using more leverage than  
he did as recently as June.

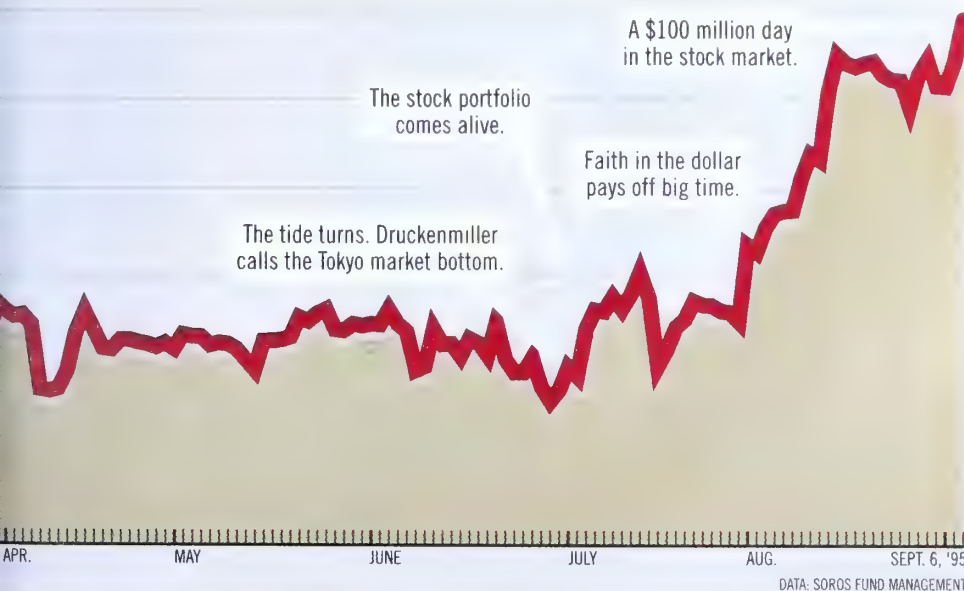
Soros' decision to go public is in con-

trast with other hedge fund managers,  
who have been largely silent. The big  
funds fell up to 30% in 1994—Quan-  
tum eked out a 3% gain—and none  
have rebounded in '95 quite so dramati-  
cally as Soros'. Such superinvestors as  
Michael Steinhardt, Leon G. Cooper-  
man, and Julian Robertson Jr. are com-  
ing back, however, and they lead a re-  
surgence among the previous laggard  
hedge funds (table, page 102).

**CHALLENGES REMAIN.** But for the  
hedge fund business in general, includ-  
ing Quantum, long-term problems re-  
main. Unless their mediocre perfor-  
mance reverses as decisively as it has  
for Soros, investors could become reluc-  
tant to pay hefty incentive fees to  
hedge fund managers—which usually  
amount to 20% of profits. (Mutual  
funds, by contrast, reinvest their prof-  
its.) Size is a problem for the largest  
funds. Fed by the gains many achieved  
early in the 1990s, size works against  
Soros and the other megafunds. Soros  
has long acknowledged this, and it has

been a particular prob-  
lem for Steinhardt, who  
is widely rumored—for  
the second time in a  
year—to be planning to  
shut down and distrib-  
ute fund assets to his in-  
vestors. He won't com-  
ment, but the rumors  
are discounted by Stein-  
hardt colleagues who say  
that the mercurial fund  
manager has ample rea-  
son to stay in business.  
(Quantum, though usual-  
ly grouped with hedge  
funds—partnerships for  
the wealthy—is actually  
an offshore mutual fund,  
closed to U.S. citizens.)

For the moment, how-  
ever, the ever-harsher  
realities of the hedge  
fund business seem far





# A chastened Soros uses old-fashioned stock-picking, as well as macro bets, to rack up recent eye-popping gains

away for Soros. His successful confrontation with the markets is far more multifaceted than merely a leveraged bet on the dollar. It also has involved jettisoning projects that seem problematic, such as a fund investing in India and a real estate venture with Paul Reichmann. According to Soros, the deal with Reichmann fell apart because Soros refused to provide financial backing for Reichmann's effort to regain his Canary Wharf project—a deal rejected by Soros, he says, because of its huge size.

**WINNING COACH.** In his interview with *BUSINESS WEEK*, the normally dour and philosophical Soros was cheerful, even elated. His new, sometimes chatty, sometimes opaque book—*Soros on Soros*—is selling well. But there was a tangible reason for his cheeriness. He had just reaped his one-day \$100 million gain, not from the kind of high-octane “macro” investing that made Soros famous, but through that most prosaic of Wall Street pastimes—stock-picking. It epitomizes the chastened, more cautious George Soros of 1995. That \$100 million gain sprang from Soros' portfolio of stock holdings, led by Burlington Northern, Chrysler, Newmont Mining, Intel, and Scott Paper.

In mid-July, as *Soros on Soros* began to cascade off the printing presses, Soros told his funds' investors that he was retreating from the big-picture, highly leveraged macro investing in currencies and bonds that had been his forté. Yet in the few weeks since the book began arriving at the stores, Soros has seen his macro strategies pay off dramatically, and has “coached” his flagship Quantum fund, by far the biggest and most successful hedge fund in the world, to dramatic gains.

Although Soros spent June tending to his philanthropic operations in Eastern Europe, particularly Ukraine, and then July and August in Southampton, he kept in daily contact with Druckenmiller and with other key subordinates—including Nicholas Roditi, the London-based trader who runs mac-

ro trading for Soros' Quota fund.

Roditi, who declined to be interviewed, has emerged as a star of the Soros organization. He steered the \$1.5 billion Quota fund to the kind of performance that distinguished Quantum in the old days—a gain of 105% in the year to date. He was in daily contact with Druckenmiller as well as Soros throughout the year, but they did not see eye to eye very much. According to Druckenmiller, at times Roditi took macro positions that were the exact opposite of the money-losing positions held by Quantum. “He was on the right side of the markets from day one this year,” notes Druckenmiller.

Quota was able to build on its gains, to risk old profits to make new profits. But Quantum didn't have that option. Even though Soros felt that his bullishness toward the dollar was basically right, he was restrained from using

leverage by his own losses. For many investors like Quantum, losing money is like a progressive disease. The more money you lose, the harder it is to take the leveraged risks that are required to help you recover—because those very risks can destroy you.

**LOST MOMENTUM.** But if you're making money, you are not risking the financial very existence, only its recent profits. It is a simple but dead-serious dilemma. “When you're losing money, it's harder to make money,” says Soros. “It was very difficult to regain momentum.” Every time a trade proved successful in the first half, it was successful enough—the leverage was minimal—and the currency markets turned sour again. Momentum was lost. “If I were to look at a chart of the asset value I'd say that we touched the break-even point at least five times and then we fell back.... But once we put our head above zero, we could move ahead.”

For Quantum, the psychological turning point came in early July. What got the fund reeling was the gain in the Japanese market, early in July, that coincided with the concerted intervention in the dollar-yen market. Fortunately for the wounded Quantum, Druckenmiller called the bottom of the Japanese market right on nose.

“That might have been a psychological bottom,” says Druckenmiller. “I think it was a confidence booster, yes. That was certainly one of the things that made us feel we were not totally incompetent around here.... We had been short [the Japanese market] and successfully avoided getting killed when it went back up. That gave us a sense of confidence to do other things”—such as take a long position in the dollar vs. the yen, and in European and Japanese bonds. Failing to call the bottom, he notes, “might have prevented us from being aggressive in some of the areas we were right in.”

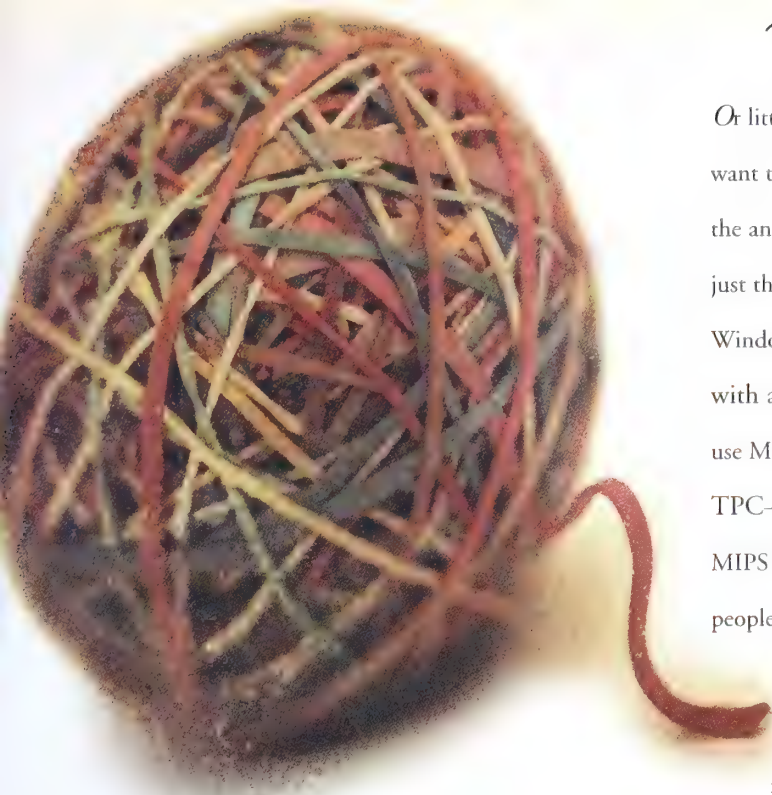
Druckenmiller is peeved about rumors that have dogged the fund, dismissing its gains as

## Hedge Funds Begin To Outpace The S&P 500

| Hedge fund category   | FIRST HALF | JULY  | AUGUST |
|-----------------------|------------|-------|--------|
| FINANCIAL EQUITIES    | 25.5%      | 5.9%  | 8.5%   |
| MACRO                 | 1.4        | 3.8   | 6.3    |
| VALUE                 | 11.6       | 1.7   | 3.0    |
| PACIFIC RIM           | -4.6       | 3.2   | 2.5    |
| INTERNATIONAL         | 4.1        | 3.1   | 2.5    |
| LATIN AMERICAN        | -10.7      | 1.7   | 2.4    |
| GROWTH                | 16.6       | 7.7   | 2.2    |
| LEVERAGED BONDS       | 8.7        | 5.8   | 2.1    |
| DISTRESSED SECURITIES | 13.1       | 3.1   | 2.1    |
| MULTIPLE ARBITRAGE    | 5.1        | 2.0   | 2.0    |
| EVENT-DRIVEN          | 10.4       | 0.1   | 1.6    |
| OPPORTUNISTIC         | 11.5       | 4.2   | 1.5    |
| RISK ARBITRAGE        | 10.5       | 1.4   | 1.3    |
| CONVERTIBLE ARBITRAGE | 13.1       | 2.0   | 1.1    |
| MARKET-NEUTRAL        | 6.9        | 1.6   | 0.3    |
| EMERGING MARKETS      | -9.5       | 3.4   | -0.2   |
| SHORT SELLING ONLY    | -18.2      | -11.0 | -0.8   |
| HEDGE FUND INDEX      | 8.3        | 3.2   | 2.5    |
| S&P 500               | 20.2       | 3.3   | 0.3    |

Hedge fund numbers are an unweighted index of 200 representative hedge funds; distributions to investors are included. Figures do not include deductions of incentive fees—usually 20% of profits—and management fees.

DATA: HENNESSEE HEDGE FUND ADVISORY GROUP AT WEISS, PECK & GREER



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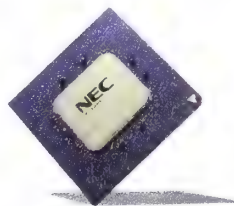
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simple-minded leveraged bet on the dollar. "Complete baloney," says Druckenmiller. "Our worldwide fixed-income gains this year are larger than our currency gains."

Soros and Druckenmiller insist that stock-picking has been as significant for Quantum lately as macro investing—an assertion certainly buttressed by the \$100 million Sept. 5 gain. Soros favors companies "where there's a change in the way the companies are managed." He cited Scott Paper as an example of a company where "management has made a tremendous difference. We are very interested in the quality of management."

**FIRST LOVE.** But macro investing is clearly his first love. The Sept. 13 gain shows that Quantum is again taking leveraged macro bets, despite Soros' decision on July 14 to cut back on macro investing. Macro investing was eliminated entirely—except as "market conditions permit"—for Soros' Quasar and Quantum Emerging funds. But with macro investing coming back, Soros now apparently feels that the conditions are right for Quasar and Quantum Emerging to resume macro trading. Now he says that "some other younger people do some macro trading" in those funds.

For Soros, macro investing is an intellectual challenge and one that he makes sound downright easy. He likens the recent situation to the period discussed in his book *The Alchemy of Finance*—the time of the Plaza accords of 1985, which allowed governments to intervene in the freely floating exchange-rate system.

At that time, Soros had a firmly held view on currencies, and it took a nudge from the central banks to help him make money. Likewise, Quantum's recent dollar bonanza stems from a passionate view that the dollar had to move up—and that a push from the authorities would send it there. What the bankers did was "to make it move in the direction where it ought to have gone by its own. How shall I say—the situation demanded it."

Clearly, macro investing will be one area where George Soros will continue to lead. "We're finally getting it right," says Soros. And how. But the early months of this year prove that even the smartest practitioners of macro investing can come very close to being knocked out for good. Soros pulled it off this time. But if the markets send him reeling once again, he may not be so lucky.

By Gary Weiss in New York

## RESTITUTION

# 'THE SWISS ARE FINALLY STARTING TO COME CLEAN'

Bankers agree to return Holocaust property and look for more

**S**ecret meetings in Bern in late August led to a breakthrough to recover millions of dollars in Jewish property held in Swiss banks since the Nazi era. The talks between the Swiss Bankers Assn., World Jewish Congress Secretary General Israel Singer, and Swiss Jewish leader Rolf Bloch resulted in a surprising Sept. 12 announcement. The bankers said that a survey of its members begun in June had so far uncovered \$34.1 million in 893 accounts opened prior to the end of World War II. The Swiss also agreed to open an office to help Holocaust survivors and heirs find lost accounts.

Jewish leaders meeting in Brussels to discuss the affair and the recovery of other Jewish property in Europe were not buying the figure. "We are concerned with the Swiss attempts to deflate the amount," says Singer.

**HIMMLER'S LOOT.** For the Jewish leaders, the search has only just begun. "We have new documents from the Stasi files and archives in Eastern Europe that we plan to present to the Swiss," says Singer. The records of the Stasi, the former East German secret police, refer to a large shipment to Switzerland of gold, diamonds, foreign currency, and paintings taken as payment by SS boss Heinrich Himmler for the freedom of 13,000 Hungarian Jews in 1945. Various estimates of the current value of the shipment range from several hundred million to \$1 billion.

The bankers had been saying until recently that the issue had been resolved in 1963, when the Swiss government ordered the banks to report all monies of Holocaust survivors. That sweep netted about \$2.2 million, which was handed over to Swiss Jewish organizations. The Swiss dispersed \$1.7

million of that to a small number of claimants.

"The Swiss are finally starting to come clean and are trying to put the issue to rest 50 years after the end of the Second World War," says Singer. And others, including WJC President Edgar Bronfman, are anticipating lengthy negotiations before any final agreement is reached. The first formal talks were begun on Sept. 14 with meetings

between a team led by Bronfman and a group of Swiss bankers and Swiss President Kasper Villiger.

Bronfman has decided to set up a special committee made up of bankers, Holocaust survivors, and Jewish leaders to deal with the search. The committee will be responsible for collecting names of individuals and companies and handing them over to the Swiss Bankers Assn. for examination.

**SEARCH FEES.** A central contact office to assist searchers will

be set up next year and run by the banking ombudsman's office, a watchdog created by the banking association. However, the bankers rejected Jewish demands to conduct searches free of charge for Holocaust survivors and heirs and said the amount of the fee is yet to be determined. Up to now, the banks have been charging \$85 to \$850 for searches, which have in most cases failed to turn up anything.

Bronfman and the WJC intend to keep pressing the Swiss. "We've waited 50 years to resolve what has become a very painful issue," Singer says. Armed with new documentation and public opinion, these Jewish representatives believe they have a better chance of setting right an old wrong.

By Neal Sandler in Jerusalem, and John Parry in Geneva



## PAPER TRAIL

Armed with newly released documentation, World Jewish Congress President Edgar Bronfman says he will keep the pressure on the Swiss

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MARKETS

## CHINA'S OTHER EXCHANGE REACHES FOR THE SPOTLIGHT

Shenzhen hopes to catch up to scandal-plagued Shanghai

**L**odged in the three-story Grand Theater building that also houses a concert hall, movie theater, and karaoke joint, the Shenzhen Stock Exchange is easy to miss. But appearances are deceiving, insists exchange President Xia Bin. Having suffered through a nine-month downturn that brought trading to a near-standstill this spring after prices plunged 40%, China's No. 2 bourse is starting to recover. Says Xia: "We've come back."

And quite smartly, at that. Daily volume in "B" shares, the class of stock available to foreign investors, has increased fivefold in just three months. Since June, the exchange's index of B shares has jumped 15% (chart). Activity in "A" shares traded by locals is picking up as well. Expectations that the central bank will ease credit is helping the market get on the road to recovery. But so is a spate of new listings from companies across China that are luring foreign investors away from Shenzhen's bigger and more glamorous rival to the north, Shanghai.

Shenzhen's rebound is an indicator of the changes afoot as China attempts to clean up its troubled capital markets.

After a year-long policy deadlock in Beijing, proponents of controlled growth of new listings have won out over advocates of rapid expansion at any cost. As a result, supervision of exchanges is increasingly being placed under the control of the China Securities Regulatory Commission (CSRC), an arm of the government in Beijing.

**CLOSE THE GAP.** The shift means that local companies, many of them property developers with shaky fundamentals but good connections to market officials, are making way for better-managed companies on Shenzhen's bourse. Since Beijing ended a ban on new listings of B shares earlier this year, Shenzhen has offered half a dozen new listings. They include Sichuan-based motorcycle maker Shenzhen North Jianshe Motorcycle, Wuxi Weifu, a manufacturer of fuel-injection equipment based in Jiangsu province, and Jiangling Motors, a truckmaker

**MOMENTUM:** Shenzhen has grown since a new-listing ban was lifted

from Jiangxi, in which Ford Motor plans to purchase a 20% stake.

The bid to go national by upstart Shenzhen, which is situated in a special economic zone developed over the past two decades, is aimed at narrowing the gap with the market in Shanghai, China's historic financial and industrial center. With a large number of local companies eager to float stock, the Shanghai market has made it difficult for companies from outside the city to gain listings. "Officials there give priority to their own enterprises," complains Ann Shih, head of China research at W.I. Carr (Far East) Ltd. in Hong Kong.

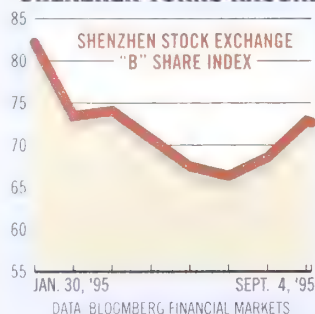
That doesn't sit well with Beijing, where the CSRC's new chief, Zhou Xiaojiong, who was appointed last spring, is determined to set the agenda for both exchanges. Some analysts wonder if Zhou will replace Shenzhen market czar Xia so he can have his own mandate. But Zhou is also likely to pressure Shanghai exchange officials. They angered regulators by protecting big local traders during a bond-futures scandal last February that nearly toppled the city's leading broker, Shanghai International Securities.

**NOT CONCERNED.** Shanghai's regulatory shortfall provided an opening for Shenzhen. But Shenzhen still has to overcome a few deficits. Since so many foreigners thought Shenzhen was dead under the water, stocks have been cheaper than in Shanghai. That difference persists even with Shenzhen's listing blitz. For instance, Jianshe Motorcycle started trading in July at 6.8 times earnings, about half that of Shanghai-based rival Ek Chor China Motorcycle. And with Shanghai remaining as the headquarters for many Chinese and overseas banks and insurers, there are some investors who doubt that Shenzhen can sustain its brand new momentum.

But for now, says, he is not concerned—about officials in Beijing or Shanghai. "China is so big," he says. "The south can have a financial center, too." There may be more daytime drama in store at Shenzhen's Grand Theater yet.

By Bruce Einhorn in Shenzhen, and Dexter Roberts in Shanghai

### SHENZHEN TURNS AROUND





# 'S NOT CALLED MIDAS OR NOTHING

by the top-ranking gold fund stays on top

portfolio manager of the Midas Fund, Kjeld R. Thygesen has developed a touch all his own. As of June 30, his tiny, \$10 million gold fund had up a 42% return, compared with an average of 6% for the 42 precious-metals funds tracked by Morningstar. The fund's dazzling return has little to do with the price of the yellow metal, silver, or even with companies mining in South Africa, the world's sin-

price in the fall, he isn't betting the farm on it.

Thygesen distinguishes himself from other precious-metals funds by investing a significant chunk of assets in speculative mining ventures. He puts 25% or so of the fund in mining and resource stocks that have made a discovery but are still in the development stage. That can mean investing in "very small-cap, new project companies" such as Canadian mining company Dia-

mond Fields Resources Inc. Diamond Fields accounts for about half of the fund's gain year-to-date. In the fall of 1994, Thygesen bought the stock at 4. When the company started drilling, it uncovered a greater-than-imagined deposit of base metals such as nickel and copper. The stock currently trades at 91.

**ON THE ROAD.** Thygesen is also finding winners in what

he calls "intermediate gold production companies," small- to medium-cap growth companies looking to expand production or acquire other companies. A current favorite is Dayton Mining Corp. The company just commenced production on a gold mine in Chile, and with costs of about \$150 to produce an ounce of gold, it can achieve a hefty profit margin even if the metal stays stuck in its present trading range, says Thygesen.

The Midas Fund focuses on North American mining stocks, but Thygesen is eyeing new investment opportunities in Third World countries. He is searching in South America, in Indonesia, in the Philippines—even in Russia and in the former Soviet states. That keeps Thygesen on the road about a third of the time, which helps push fund expenses above the 1.7% average, to 2.1% of assets. The ratio should fall as the assets of the fund increase. And with a gain of more than 40%, current shareholders probably aren't too concerned about Midas Fund's expense ratio.

By Suzanne Woolley in New York

## MINING FOR HUGE RETURNS



largest gold producer. Thygesen finds the biggest winners by venturing off the beaten path, into the jungles of Namibia, or the waters off Namibia, in the pursuit of small-cap mining companies he thinks will hit it big.

Precious-metals funds are notoriously volatile, winding up at the top of the market one quarter only to be at the bottom the next. But the success of Midas Fund, formerly called Excel Midas Gold Fund, is no flash in the pan. It is the top-performing precious-metals fund for one-year, three-year, and five-year periods ending June 30, 1995, according to Morningstar. With such statistics in hand, Thygesen hopes to build assets to \$100 million by 2000. Recently, the fund dropped its 4.5% load.

**STILL IN DEMAND.** The Midas Fund may be classified as a gold fund, but Thygesen stresses that it is a "mining growth fund, too." That's a good thing, since the price of gold has been static for the last two years, ranging from \$375 to \$400 an ounce. While Thygesen expects continued demand for gold in Asia and Japan to contribute to "a pop" in the gold

# HOT TRANSCRIPTS

Missed the chance to talk with Netscape co-founder **Marc Andreessen** when he was the guest of a Business Week Online live conference? Or maybe you were away when BW economist **Bill Wolman** gave his latest investment advice.

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BY GENE G. MARCIAL

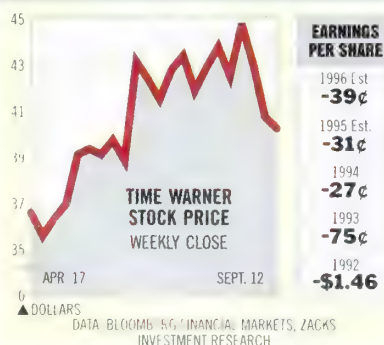
## CASHING IN ON TIME AND TURNER

**H**ow does an investor play Time Warner's (TWX) proposed takeover of Turner Broadcasting System (TBS/B) now that it seems hung up on maneuvering by insiders? Will there be a deal, or will John Malone, who heads Tele-Communications (TCOMA), which owns 21% of Turner, torpedo it? What about General Electric (GE), which owns the NBC Television Network? Will it go after Turner?

Rumors abound, and bets are everywhere. But several major stakeholders close to players in the talks are convinced that: (1) Turner will, indeed, be acquired by Time Warner—sooner rather than later, and (2) GE will sell NBC, valued at \$6 billion to \$8 billion, to the Time Warner-Turner enterprise for stock that could give GE a 15%-to-20% stake in the new media-broadcasting-entertainment giant.

"Buying NBC from GE for stock would provide Time Warner-Turner a capital-rich partner in GE, which could bolster the new combination's cash flow and also enable it to accelerate a much-needed deleveraging process," says Herb Ehlers, president of Liberty In-

### TURNER MAY MEAN A TURNUP



vestments Management, which owns 2.4 million shares of Time Warner, 5.6 million shares of TCI, 1.6 million shares of Liberty Media (LBTYA), the TCI affiliate that owns the 21% stake in Turner, and 700,000 shares of Turner. As a big stakeholder, Ehlers is close to the big players, including Malone. A spokesperson for NBC says it isn't for sale but is interested in strategic alliances.

"Apart from the valuable assets of NBC, GE brings to the table its deep

pockets," says analyst David Shell, also of Liberty Investment, "which could be the source of badly needed cash for Time Warner in its quest to deleverage, particularly after acquiring Turner." A GE spokesman declined comment on rumors about buying Turner or Time Warner.

Shell notes that, except for Turner, the other "significant beneficiaries" in this evolving drama have yet to reflect the full value of the deal in their shares. Turner shot up from 24 a share to 30½ on Aug. 30, when Time Warner announced its tentative pact to acquire the 82% of Turner that it doesn't already own for \$8 billion (35 a share) in stock.

Since the announcement, Time Warner has slipped from 42½ to 40. Ehlers says it's undervalued by at least 50%, based on the Turner acquisition and other potential deals ahead.

Other beneficiaries whose stocks haven't reacted and that Shell thinks are great buys: TCI, which has edged up only from 18½ to 19, and Liberty Media, whose stock hasn't budged from 26.

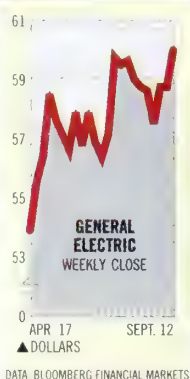
GE, another potential winner, also hasn't reacted much—it's at 60. GE is way undervalued, says Shell, especially if you throw in the prospects and potential value of NBC.

## IS THAT GE IN THE REARVIEW MIRROR?

**N**ot many have heard of Research Frontiers (REFR), but its shares spiked up from 8½ to 13½ in one day, on Aug. 2. The reason: It announced an agreement licensing GE to make films incorporating the company's proprietary technology in electrically operated light-control devices. Some corporate insiders were quick to sell after the leap. But some pros have stayed on.

Why? They sniff a takeover. "There were big-block buyers of the stock, and I suspect one of them was GE," says Ignatius Teichberg, editor of *Teichberg's Market Strategy*, a newsletter that specializes in scouting takeover targets. A recent hot takeover pick was Bank

### EYEING A BIGGER SHOWBIZ ROLE



South which he first recommended 13. On Sept. 5, NationsBank agreed to acquire Bank South for 27.

He thinks GE is accumulating R search shares. "I don't think GE will stay a passive partner," says Teichberg, who first recommended the stock when it was at 4½. He says: "Ultimately, GE will buy the company, which is worth 25 in a buyout." Research President Bob Saxe says he's unaware of any buying by GE. And a GE spokesman says GE doesn't own any of the shares.

Research Frontiers has yet to make 1¢, Teichberg notes, but GE isn't the only believer in its "suspended-particle device" technology, which incorporates a light-sensitive film between two pieces of glass. It's used in flat-panel displays for computers and TVs, eyewall self-dimming auto sunroofs, sun visors and rear-view mirrors."

Among other licensees: Sanyo Electric of Japan, Glaverbel of Belgium and Japan Steel Works. Saxe expects one of the licensees to market a product next year using the technology.

## OLIN MAY HAVE ITS FORMULA RIGHT

**O**nce a laggard in chemicals, Olin (OLN) has been a highflier of late. Its stock hit a new peak of 71½ on Sept. 12, in part because of upbeat recommendations by a couple of Street analysts. Rising demand for chemicals and brass, they note, improved the outlook for Olin, which makes electrochemicals as well as metal products used in coins, ammunition, and electronics. But says one New York investment manager, there's another factor behind the surge: a big restructuring that includes sale of important assets.

One investment banker puts the private-market value of Olin's assets at \$130 a share. The unit that provides the highest profit margin among Olin's three operations is the metals group, he notes, producing copper, copper alloys, and fabricated products. Metals could well become Olin's core division after the restructuring, he says.

Management is said to be shopping its aerospace-defense operations. Olin had attempted last year to form a joint venture of this unit with Alliant Technology, a maker of rocket engines and ammunition, but the Justice Department nixed the idea. The talk is that Alliant may make a bid to buy the unit. Olin declined comment.



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# PCs: THE BATTLE FOR THE HOME FRONT

When the dust settles, which manufacturer will rule the family market?

**S**ick of Microsoft Corp.'s Windows 95 blitz? Tired of nonstop ads for multimedia this, online that? Bored by friends and associates who boast about their hot new Pentium PCs and the cool new Web sites they're finding on the Internet? Too bad. The fall personal computer season is just beginning, so between now and Jan. 1, the world's PC makers will be blanketing the mails, the airwaves, and newspapers and magazines with hundreds of millions of dollars' worth of messages aimed at getting some 3.6 million Americans—and 1.6 million Europeans—to buy new PCs.

The market for home PCs, which has been the hottest growth segment of the computer business for two years, is now a critically important battleground for PC makers. They rely increasingly on fourth-quarter sales to consumers to achieve their yearly numbers—and to make up for slow growth in their other markets. Compaq Computer Corp., the biggest PC maker of all, has built a \$3 billion business in home computers from scratch since 1993, and companies from IBM and Digital Equipment to Hewlett-Packard are eager to do the same. That's what's behind a massive yearend push to get experienced PC owners to trade up and convince a wider swath of the public that it's time to bring the Information Age into their homes, too.

**"PRETTY COOL."** The season is already off to a roaring start. It began with the Aug. 24 introduction of Windows 95, prompting millions of PC owners to consider buying replacement machines, and continued with stronger-than-expected back-to-school sales. Says Edward R. Anderson, chief executive of Dallas retailer CompuCom Systems Inc.: "It was like a gun went off in mid-August, and sales picked up." In September, Compaq, IBM, Acer, Hewlett-Packard, and Dell Computer added more fuel with new consumer models featuring everything from special chips for running video to stylistic flourishes

to make a PC look at home in your living room.

Will it work? Industry analysts are busy ratcheting up their fourth-quarter sales forecasts. They're now figuring shipments will jump as much as 30%, not just the 20%-plus surge they had predicted earlier (chart). PC factories are running on overtime. And television is beginning to groan under the weight of PC advertising. The message takes many forms, but there's a common theme: The PC is the all-purpose home-entertainment gadget, a stereo for pumping out the music of the latest compact disk, a video-game machine for Doom fanatics, and a cybercruiser for every member of the family.

For experienced PC users, it isn't such a hard sell. "This is a product whose abilities keep multiplying," says Andy Bose, vice-president at Link Resources Corp. This year, for example, one of the hottest-selling options on Gateway 2000 computers is a changer for stacking audio CDs. Such features helped persuade college freshman Chris R. McFarlen of Arlington, Tex., to plow \$3,000—everything he could scrape together from a summer job at a phone

company—into a Dell Computer Corp. 100-megahertz Pentium PC, with a CD player, graphics and sound cards, a 17-inch monitor, and an ultrafast 28,800-bit-per-second modem to cruise the Internet. "It's pretty cool," raves the

The season is already off to a roaring start, thanks not only to Win95 but also to new models featuring everything from multimedia-friendly chips to chic designs



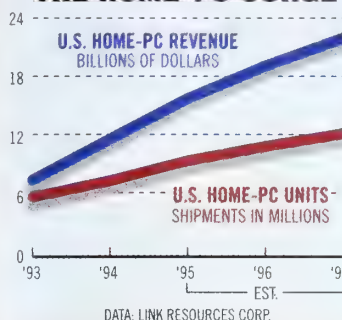
ne Christian University student. faster, and you start getting able." The tricky part for PC makers will be generating that kind of enthusiasm among millions of new consumers. Until the market has largely been upper-middle, white-collar families (most PC households have annual incomes exceeding \$50,000). To reach this year's sales goal, the market has to broaden. Link Resources predicts nearly 17% of home-computer buyers in the next 12 months will be new consumers, compared with 10% in previous years. Forrester Research Inc. says the fastest-growing segment of the market will be families earning from \$10,000 to \$50,000. Reaching these new customers will require savvy consumer marketing

skills. "Brand name matters more and more," says Digital Equipment Corp. Vice-President Howard Elias. That's one reason why IBM and Compaq this year tapped consumer marketing specialists to lead their home-PC pushes. Mass merchandisers are enthusiastically joining in, too—loading up on inventories of what has now become the hottest category in consumer electronics. Bradbury H. Anderson, president of electronics chain-store Best Buy Co., says PCs now account for 38% of the Minneapolis company's sales, up from 26% two years ago.

**LESS TECHNOBABBLE.** A bigger market also means providing a level of service that PC makers aren't accustomed to. "Support is weighted highly in terms of value," says Gateway 2000 Inc. marketing director Al Jiazzon. As Microsoft Corp. has already discovered with Win95, when you suddenly whisk neophytes into the disorienting world of computers and computerese, you have a lot of handholding to do. Despite painstaking preparations, Microsoft found phone lines flooded with 20,000 calls a day from Win95 buyers (page 114).

Apple Computer Inc., long the No. 1 supplier of home PCs and now No. 2 behind Packard-Bell Electronics Inc., is hoping to bounce back by de-emphasizing all the technobabble that can turn off new buy-

## THE HOME-PC SURGE



ers. "It's not going to be with a PC-centric approach because these people aren't interested in learning about PCs," says Apple Chief Executive Michael Spindler. Apple has new, lower-cost Macintoshes and has added features such as one-button Internet access. It has special Mac packages for different types of consumers, and an Apple ad blitz will stress the Mac's simplicity.

Still, Apple could be in for a disappointing Christmas. Consumers may indeed respond to Apple's claims that Mac remains the easiest computer to use—and won't pose the kind of shake-down problems buyers may encounter with Win95. But the Cupertino (Calif.) computer company made a costly miscalculation: It underestimated, by as much as 40%, demand for certain key components and will be hard pressed to get enough machines onto store shelves this fall. Alan Bush, chief executive of Tandy Corp.'s Computer City chain, predicts that the shortage will cost Apple dearly. "I believe the top three selling brands will be Packard-Bell, Compaq, and HP," says Bush.

**BEST BEHAVIOR.** IBM could also find itself on thin ice. Retailers were burned last Christmas when Big Blue failed to ship sufficient numbers of its Aptiva PC line, and many consider IBM on probation: If it can't deliver hot-selling machines in sufficient quantities this season, they'll make room for other brands, such as NEC Technologies and HP. IBM seems to be on its best behavior. It brought out a new line of Aptivas on Sept. 11 and, to keep dealers happy, began shipping supplies a month in advance. To attract customers, it's buying ads on everything from *Monday Night Football* to *Seinfeld* and pushing features such as standard 28.8-baud modems (vs. the usual 14.4), new video capabilities, and "theater-quality" sound. "It's a great interactive gaming and learning experience," says Consumer Div. Marketing Vice-President Michael Parides, recently lured to IBM from Compaq.

Compaq, which introduced a new line of home PCs on Sept. 13, is pulling out the stops to grab the market lead from Packard-Bell Electronics Inc. It began attacking the home-market leader's credibility last spring by filing a suit claiming that the Westlake Village (Calif.) manufacturer fraudulently resold returned computers as new ma-





chines. Now, Compaq is launching a \$40 million TV and print ad campaign touting higher-quality video and sound.

Compaq is lavishing more and more attention on the home market, which is growing two to three times as quickly as the business-PC market. It has set up a special laboratory where researchers observe consumers using prototype machines in various situations—an apartment, an office, and on an airplane. Compaq also is working with Mattel Inc.'s Fisher-Price to develop computers that resemble toys, for 4- to 7-year-olds. Michael Heil, a former Sony Corp. executive, who recently became senior

top of Windows 95 and lets customers organize their applications in groups represented by icons—for games, finance, and so on.

Another way to differentiate is to move beyond the standard putty-colored PC box. Acer America's new Aspire home-PC line, introduced on Sept. 5, for example, boasts a curvy design in decorator green and charcoal that "breaks the Model T mentality," says Acer President Ronald Chwang. Packard-Bell also has new shapes—a wedge for corner locations and a low-profile pizza-box computer. "We think style is a factor," says Packard-Bell's Ransom.

This is not to say that the feature wars are over. Compaq, for example, will be trying to convince customers that the video in its new Presario—produced with special video-process chips—is superior to video on Packard-Bell machines, which rely on special software to compress and play back video data. IBM, on the other hand, uses a combination of software and hardware for video. The challenge, says Compaq product marketing director Mark Vena, is that "70% to 80% of our customers don't know what MPEG [video compression] is."

Whether or not consumers know—

care—how the sound and music got there, they like multimedia PCs. And Windows

represents a great leap forward in multimedia. That's what sold David J. Clark, a St. Paul (Minn.) security supervisor, the new operating system. "I decided I wanted a play-it-and now that I got one, I spend most of my time on it," he says. The lure of multimedia also snagged Carol Jones, a Santa Clara

(Calif.) administrative assistant who just bought a \$2,000 Mitac PC "that's going to take me to the 21st century."

**SHORTAGES.** Between upgraders and the newcomers to the market, the biggest concern among makers is keeping up demand. "It's a great world to have, isn't it?" says Dell Computer Corp. CEO Michael S. Dell. With demand unexpectedly high this season, there are industrywide

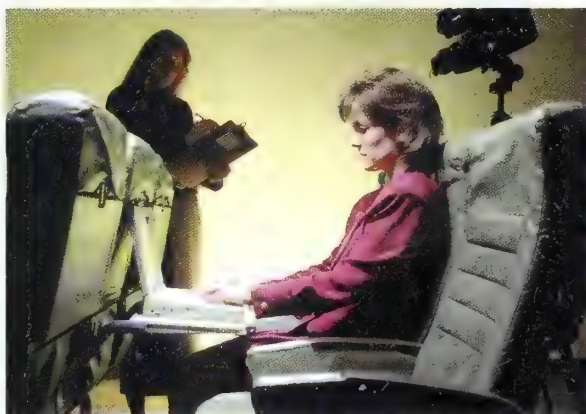
shortages of components such as memory chips and disk drives. That is keeping prices firm. So new features that are raising the average selling price of home models by as much as 2% to 5%, says PaineWebber computer analyst Michael Kwatinetz.

But how long will the party last? PC makers

## Tweaking the Personal Computer

### AIRWORTHY

Compaq Computer simulates the confines of a jetliner at its Human Factors Lab



**DO THE DISHES?** Packard-Bell, meanwhile, is sticking to the strategy that gained it the leading share last year: Give consumers the most "stuff," says Mal D. Ransom, marketing vice-president. In addition to all the multimedia features of last year's models, Packard-Bell's fall line includes such

goodies as a remote control that can turn on the CD, control volume, and retrieve phone messages from the PC. Packard-Bell also offers direct access to its own private-label Internet service.

New techno-gizmos and splashy features may not be what's needed to push PCs into a wider market, though.

When it comes down to it, there's not much difference between one 100-MHz Pentium machine and another. PC makers, therefore, are seeking other ways to differentiate their wares. One is through software to insulate the neophyte user from some of the ugly realities of running a computer. Hewlett-Packard, new to the home market, throws in a program called Personal Page that rides on



**DECOROUS** Through the new hues of its Aspire line, Acer aims to "break the Model T mentality"

### FRIENDLIER

HP's new toon-laden personal page tries to draw in the whole family





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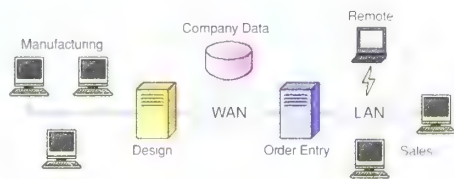
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say the computer's ability to absorb more and more functions of other consumer-electronics devices will keep expanding the market and prompting upgrades. Yet the penetration rate—expected to hit nearly 50% of American homes by 1997—is going beyond the levels where sales of electric typewriters and video-game machines began to slow.

Researchers are predicting that the home-computer market will cool off, slowing to a 16% growth rate in 1996 and 12% in 1997. Bose of Link Resources figures that growth “will hit a wall when penetration gets to 65%.” Then PC makers can achieve respectable growth by focusing their efforts overseas. “On a global basis, people say this is a device that will be important in

their lives,” Bose says. Indeed, market researcher Dataquest Inc. predicts the home-PC market in Europe should jump 49% this year. In other words, the home-PC blitz will remain a high-tech holiday ritual for years to come.

*By Gary McWilliams in Houston with Peter Burrows and Kathy Rebello in San Francisco, Larry Armstrong in Los Angeles, and bureau reports*

## START ME UP—JUST TRY

*If you start me up,  
If you start me up, I'll never stop*  
—Rolling Stones

**T**alk about mixed blessings. Microsoft Corp.'s advertising blitz for Windows 95 is a major success. Slick images and the beat of the Rolling Stones singing *Start Me Up* have convinced hordes of buyers that computing just got a whole lot easier. Win95 sales boomed to a record 1 million copies in just four days and triggered strong demand for new computers and other software.

There's a catch, though. It isn't just the nerdy “early adopter” crowd that's snapping up the new PC operating system. And the less savvy buyers are finding that Win95 doesn't quite make computers easy enough. After three weeks, Microsoft's “help” lines are still jammed with callers who need assistance with simply installing the new software. The more vexed of them are posting another line from the Stones song on various message boards: “You make a grown man cry-y-y!”

**WIT'S END.** John J. Bunish of Ogden, Utah, an Air Force major who has used computers for years, dashed out to buy Win95 in the belief that his 5-year-old son would find it “quicker and easier” to use than Microsoft's earlier Windows program. Installation went fine, but Win95 actually made Bunish' PC run some of his son's game programs either slowly or not at all. After two nights of fiddling, the boy was in tears and the father out of patience. Bunish returned the software. “The best thing” he says, is that Win95's “uninstall” feature works perfectly.”

To be fair, Bunish' tale may be rare. Larry Mondry, CompUSA's executive vice-president for merchandising, says that less than 1% of the Win95 boxes sold by that retail chain have been returned. But since Aug. 24, when Win95 hit the shelves, Microsoft's lines have been ringing off the hook, even with 1,600 extra support personnel, many at five outside firms, on hand. Early on, many call-



**BUSY, BUSY:** Microsoft support technician

ers got busy signals—or waited on hold for up to 75 minutes. Microsoft's own ratings of its customer service dropped from 95% to just 77% of callers satisfied.

Could Microsoft have prepared better? Its executives say there was little more to be done. Adding any more people would have meant layoffs after peak demand had passed. “It's like when the Olympics comes to Atlanta,” says Deborah Willingham, Microsoft's vice-president for support. “Do you build extra hotel rooms that won't be used when the Olympics are over?” Now, Microsoft is shifting more staff to weekends and the 8 p.m.-to-midnight shift. The result: only sporadic busy signals on

weekdays and weekend waits of less than 60 seconds, the company says.

Yet the number of calls remains at nearly 20,000 a day, in part because many novice customers still need lots of help with Win95. Some are so nervous that they won't even begin the installation process until they have a Microsoft technician on the phone. But, says Fletcher Ernst, who's helping answer those calls: “I show them

something, and they go: ‘I get it. Eureka!’”

**HIT SHOW.** To be sure, Microsoft's Win95 marketing campaign is aimed not only at the well-seasoned computer crowd but at millions of novices. The software giant is spending nearly \$200 million on promotions, including a nationwide, 30-minute “info-show” narrated by *E.R.*'s Anthony Edwards. That alone attracted an estimated 10 million viewers, many of them newbies. “That was the whole goal,” says Jonathan Lazarus, a Microsoft vice-president, “to get people to purchase soft-

ware who hadn't been comfortable with it before.”

People such as Jan Norton of Los Angeles, for instance. As a consumer marketing consultant, Norton knew computers but had never bought a new operating system before. Based on Microsoft's pitch, she reckoned that installing Win95 would be a snap—“like going out and buying myself a \$97 blouse or a hot-fudge sundae.” In fact, it took more than four days and the help of a technically minded friend. But now that Win95 is running smoothly? “I love it,” Norton says. “I do. I have to admit it.” Music, no doubt, to Microsoft's ears.

*By Kathy Rebello  
in San Francisco*

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# GLOBAL

**E**veryday business news tends to be made in a handful of countries. People everywhere sit up and take notice when Japan, the U.S., or Germany tinkers with interest rates or a high-profile finance minister kicks off a new economic program. Even the turf we call "emerging markets" often seems con-

still considered exotic by money managers in London or New York.

The surprise in these stories is that while fundamental shifts in national policy often laid the groundwork for economic growth, success has come largely through local initiative. In many cases, breaking free from long traditions of protectionism and regulation has allowed regions to prosper even faster than the nations to which they belong. For example, in China, average gross domestic product per capita is still only around \$300. But in the country's reform-minded provinces, rapidly becoming a factory to all of Asia, per capita GDP is close to \$3,000.

Still, there's no underestimating the importance of national events, such as the collapse of communism in

## Special Report

fined to a few countries that have caught the attention of investors in the past five years with a rush of privatizations or a fledgling stock index that suddenly soars.

But the world economy is vaster and more complex than that. Tectonic changes in political regimes, more open flows of trade and capital, and the spread of information technology have fostered thriving new businesses, often in remote corners of the globe. Author and former McKinsey & Co. international consultant Kenichi Ohmae writes that today's "natural business units" are increasingly cities or regions rather than nation-states. In the following pages, BUSINESS WEEK tours some of the world's hottest growth spots—many

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**AUCKLAND NEW ZEALAND** By throwing open their markets, the Kiwis are riding the Asia boom to wealth *Page 117*

**SUBIC BAY PHILIPPINES** Since the U.S. Navy moved out, trade-hungry multinationals have been moving in *Page 119*

**OULU FINLAND** This remote Arctic outpost is home to some of the world's most advanced telecom companies *Page 120*

**BOMBAY INDIA** Competition is forcing the huge B-movie industry to learn about special effects, marketing, and profits *Page 122*

**NEW YORK CITY USA** A gritty Manhattan neighborhood has become the mecca of "new media" companies *Page 125*

**SOWETO SOUTH AFRICA** Shopping centers, bookstores, and cinemas are sprouting in the former black township *Page 126*

Russia or the end of apartheid in South Africa, that provided the raw material for zealous individuals to forge into greater wealth. Our sampling of global growth spots leads off with New Zealand, a country where a radical economic overhaul in the past five years has produced a model of unfettered growth. But grassroots entrepreneurs are busy creating prosperity from the Arctic Circle to Soweto.



# HOT SPOTS



## AUCKLAND, NEW ZEALAND

### The Kiwis Are Open for Business

standing in the checkout line at a supermarket in Pakuranga, a middle-class suburb of Auckland, Kathy Parker says her life is much easier these days than when she graduated from college seven years ago. Back in 1984, Parker and her husband, Jim, had sold down four part-time jobs between them to make ends meet. Now,

Jim, an architect, is enjoying the fruits of booming demand for new housing, thanks to a surge of new immigrants.

The Parkers are not the only Kiwis to benefit from the revolutionary reforms carried out by David R. Lange's Labor government in 1984 and continued by the National government of James B. Bolger, who took office in 1990. The re-

forms have turned the nation into a sort of laboratory for free-market experimentation. New measures completely overhauled the economy, dismantling a complex set of subsidies, prohibitions, and tariffs—originally intended to protect domestic industry but in effect keeping New Zealand's economic growth and trade far below almost all other countries of the Organization for Economic Cooperation (OECD) during the 1970s and early 1980s. Now, New Zealand's economy is one of the world's least regulated and most competitive, with the growth rates to prove it (chart, page 118).

Fiscal and monetary discipline has

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New Zealand is riding a new wave of tourism and investment from Asia





## Special Report

held inflation to a legally prescribed range of 0% to 2% and helped keep the New Zealand dollar strong since 1993. The federal budget is running a surplus of \$1.8 billion, or 2.8% of gross domestic product. That ratio is expected to rise to 7% by June, 1998. And private investment as a percentage of GDP doubled from 1987 to 1994, as the combination of fast growth and low inflation made New Zealand assets highly attractive.

**JOBS RESURGENCE.** There's certainly plenty to buy. As part of its economic program, the government has been selling state-owned assets to anyone with cash. It also relaxed restrictions on foreign ownership in New Zealand companies. Between 1988 and 1994, about 30 government-run companies and agencies were sold off. For example, Ameritech, a consortium of U.S. telecom companies that includes Bell Atlantic Corp., took over New Zealand Telecom Corp. And

National Australia Bank Ltd. bought majority stakes in the formerly state-owned Bank of New Zealand.

Foreign investors are snapping up private companies, too. Food processor Watties Industries Ltd., a household name in New Zealand, was taken over by H.J. Heinz Co. of the U.S., which plans to make the Kiwi company the core of its Asia-Pacific operations. International Paper Co. bought 50.1% ownership in Carter Holt Harvey Ltd., New Zealand's largest plantation forest owner and one of the largest forest- and building-products makers in the southern hemisphere. And many motels and supermarkets are now operated by small Asian companies.

Still, New Zealand's turnaround was

### PRIME TIMBER

Foreigners are snapping up the country's huge forest-products industry

far from painless. Economic recovery in New Zealand's principal export markets from 1985 to 1987 offset the earlier effects of deregulation. But from 1987 to 1991, when nearly all farm subsidies were scrapped, unemployment reached a historic high of 11%, and many farmers were forced to foreclose.

Now, manufacturing is picking up slack. In a country that for decades depended on exports of lamb, beef, and dairy products, the manufacturing sector accounted for only 2.7% of GDP in 1987. By 1994, its contribution had surged to 25%. Overall unemployment dropped to 6.5% last year and is expected to fall further. According to the Treasury Dept., jobs will rise faster than growth in the labor force in the next two years. Manufacturers are bullish on the future as capital spending shows—up 40% in fiscal 1995 over the previous year.

**LOOKING EAST.** New Zealand also has broadened its export markets, becoming less dependent on Mother Europe. Exports to the European Community fell from 62% in 1966 to 15% in 1994, while Asia has emerged as the largest market for Kiwi products. "We are no longer Britain's overseas farm," says Peter Lund, investment promotion officer at the Ministry of Foreign Affairs & Trade. That's in part because New Zealand's latest investors often are aiming at Asian customers. Japan's Shiseido Co. has built a plant in Auckland to manufacture cosmetics for the Asian market, and J.A. Itham Foods Inc. set up a new company to produce the grain-fed beef that appeals to Japanese love.

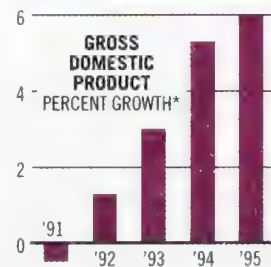
Indeed, with Asia accounting for more than 50% of New Zealand's trade and a steady inflow of Asian immigrants, students, and tourists, the country's economy will largely be shaped by the economic environment in such countries as Japan, Korea, and Taiwan. For example, Korea has now overtaken Britain as New Zealand's No. 4 export market. In August, according to Michael Stevens, vice-chairman of the New Zealand Overseas Business Council in Wellington, senior executives from Korea's Hyundai Kumho, and Daewoo groups visited New Zealand to scope out new investments.

The trend has some Kiwis uneasy. Lowerers of Winston Peters, founder of the nationalistic New Zealand First party, believe the government should not let foreigners run away with so many assets. Others, such as Jim Anderton, head of the center-left Alliance party, want to increase welfare spending and roll back some market-oriented reforms. But most Kiwis have probably come too far out of the days of high unemployment and corrosive inflation to turn back now.

By Laxmi Nakarmi in Auckland and Wellington

### NEW ZEALAND'S RECIPE FOR SUCCESS

- Selling off state assets, including the telephone monopoly and forestry cutting rights
- Abolishing subsidies and import controls
- Restricting collective bargaining to allow more labor and wage negotiations on a company-by-company basis
- Requiring the central bank to prevent annual inflation from rising above 2%
- Turning a \$1.6 billion federal deficit in 1991 into a surplus of \$1.8 billion in 1995, through government spending cuts



\*FISCAL YEAR ENDING MARCH 31  
DATA: NEW ZEALAND INSTITUTE  
OF ECONOMIC RESEARCH



## SUBIC BAY, PHILIPPINES

# Port Prospers Civvies

itors to Richard Gordon's office can't miss the photo of him fishing with Philippine President Fidel V. Ramos. The caption underneath says, "Fishing big fish at Subic."

a pretty good description of what the chief of Subic Bay Freeport is doing these days. Federal Express, AT&T, Enson and Acer are just a few of the companies that Gordon has pulled into the former U.S. Navy base. Since the Philippines launched the free-trade zone in 1992, pushing out American troops, it has attracted more than \$1 billion, becoming one of the hottest investment sites in

ability to cut through the torturous red tape of Southeast Asia. Subic allows unlimited duty-free imports and a hassle-free export system. "It's really very impressive, and as fast as Taiwan," says Kenny Wang, deputy general manager of Taiwan computer giant Acer Inc.'s plant in Subic.

### BIG HAUL

An ex-U.S. base, Subic is luring the likes of Acer and AT&T

How fast? Two weeks after Acer opened its \$24 million factory in a former cold-storage facility, it exported 3,200 computer



"Subic has acquired a life of its own," says the 50-year-old former mayor of Olongapo, the town just outside the gates.

Foreign investors see a lot that pleases them. They rave about the port's natural harbor, its modern infrastructure, and the large pool of skilled, English-speaking laborers who work for a minimum wage of about \$6 a day. That's far lower than in Singapore and Hong Kong. Subic's office space, land, and cost of living are a bargain, when compared with those rivals. Other attractions include unlimited profit repatriation and low corporate taxes.

But the biggest draw of all is the

motherboards. Now, the world's No. 7 computer maker is planning to build complete PCs and open a global repair center at the port. Acer's Subic unit will have annual sales of \$200 million in 1996, its first full year of operation. If all goes according to plan, in five years it will employ more than 19,000 people and record annual sales of at least \$1 billion.

**GAMBLING, TOO.** Such dynamism is evident everywhere. In a converted Subic warehouse, a Taiwanese company pumps out 180,000 pairs of Reebok shoes a month. In September, FedEx will begin flying daily from a former Navy airstrip up the road—part of a \$100 million project to turn Subic into its regional hub. Another Taiwanese group is putting up a 750-acre industrial park for companies that will make everything from garments to food.

Meanwhile, Malaysian gaming company Metroplex Berhad is doing a booming casino business, and its hotel is booked solid on weekends for months in advance. As more resorts go up, Asian tourists are expected to rush to enjoy Subic's clean air, blue water, and recreational activities that range from golf to hiking through virgin rain forest.

Taken together, the investments are not only reviving the port but giving a boost to a growing economic recovery in the Philippines, which is trying to erase its image as the deadbeat of Asia. When the free port opened in 1992, the country's gross national product was growing at 1% a year. This year, growth is expected to reach 6%. Foreign investment in the Philippine stock market has jumped 322%, to \$2.4 billion last year.

To be sure, growth on this scale has created some problems. Subic's supply of suitable buildings for factories is running low, as is the pool of skilled labor. Many of the 42,000 base workers who lost their jobs when the Americans left were trained for ship and port operations, not sewing shoes and waiting on tables. It can also be difficult to get around. The road leading to Manila is winding and narrow. During the four-month wet season, it's often choked with volcanic ash from the 1991 Mt. Pinatubo eruption. The drive to the capital some 50 miles away takes at least three hours—longer if it rains.

The port is trying to tackle these difficulties. A new company called First Philippine Infrastructure Development Corp. is building a \$21 million highway that will connect the base to a planned \$500 million Subic-Manila expressway. The project is expected to be completed in 1998. The base authority has launched programs to retrain prospective employees. And Gordon also says skilled workers from surrounding areas have be-

### LIFE'S CHEAPER AT SUBIC

| ITEM                  | SUBIC  | SINGAPORE |
|-----------------------|--------|-----------|
| QUART OF ORANGE JUICE | \$1    | \$2       |
| CUP OF COFFEE         | \$1    | \$3       |
| LOCAL NEWSPAPER       | 0.25   | 0.45      |
| FOREIGN NEWSPAPER     | \$1.40 | \$2.10    |
| BUSINESS LUNCH        | \$15   | \$23      |

DATA: BUSINESS WEEK



gun gravitating to the base for jobs.

While handling Subic's growth is challenging, the task seems to pale compared with the turnaround Gordon and others undertook after the U.S. Navy left its largest overseas military installation in November, 1992. The Philippines officially launched the free port the very day U.S. troops left. Gordon galvanized local support by convincing townspeople their fate was tied to the base. Some 8,000 volunteers toiled to keep the base in working order, guard its facilities from would-be looters, and show potential investors around.

**HEARD IT BEFORE.** After the World Bank pitched in with a development plan and a \$40 million loan for infrastructure development, Gordon began circling the globe. He peddled the plan to skeptical investors already tired of hearing about

## Special Report

"economic miracles" in the Philippines that never quite took off.

Two early investments helped. Enron Corp. in Houston sank \$115 million into a joint venture with Rizal Commercial Banking Corp. and House of Investments, two companies owned by Alfonso Yuchengco, Philippine ambassador to Japan. The venture runs the base's 16-megawatt power plant and a new 116-megawatt facility. And AT&T entered a venture to install and run an international communications gateway.

Regional politics also played a role. Taiwan was looking for an investment site to hedge the money it was pouring into mainland China. After an intense lobbying effort by the Ramos administration, many Taiwanese found their alternative at Subic. Taiwan's official development bank lent \$23.5 million to help develop an industrial park. Now, Taiwanese companies make up about one-third of the 181 with committed investments in Subic. Gordon is hoping Hong Kong's reversion to China in 1997 will help woo companies, too.

Subic will get a major boost in November, 1996, when it hosts the Asia-Pacific Economic Cooperation forum. The Philippines hopes to showcase the port's development during the meeting of leaders from the 18 APEC countries, including the U.S., Japan, Canada, and Australia. The summit may raise Gordon's personal profile, too. While he says that developing Subic is his first priority, he is often mentioned as a possible candidate in the 1998 presidential elections. If he keeps reeling in the companies at the port, he may soon have bigger fish to fry.

*By Michael DiCicco  
in Subic Bay Freeport*

## OULU, FINLAND

# In the Cold and the Dark, High-Tech Heat



It's a long trek to Oulu, Finland, a Nordic village some 800 kilometers from Helsinki and only 230 kilometers from the Arctic Circle. But this outpost attracts a stream of visiting Japanese and American technology execs. Some even stay for good, despite the long winters. The attraction: Oulu Technopolis, the world's northernmost science park and home to the world's best telecommunications and electronics technology.

Oulu's success is the result of years of planning. Since the early 1980s, Finland has pushed to make high technology the center of its economy, replacing wood pulp and paper products. Cellular-phone star Nokia Corp., whose stock has risen over 2,000% since 1992, is the country's best-known success story. But it's only one of many Finnish technology pioneers. Oulu alone has 100 startups in fields from software and sensors to optoelectronics and lasers, generating more than \$1 billion in annual sales.

Today, nearly a fifth of Finland's exports are high-tech gadgets, up from only 4% a decade ago. The nation's new gloss was partly obscured by a painful recession and brutal economic restructuring in the early 1990s. Deep cuts in the welfare state and corporate downsizing left 20% of the labor force jobless. **TURNAROUND.** Now, while unemployment remains high in basic industry, technology companies are expanding rapidly.

That, combined with a turnaround in paper and pulp, is expected to boost Finland's gross national product by 6% a year—the strongest growth rate in Europe. The Finns meanwhile, have the world's second strongest currency for the past 18 months, after the Finnish's turnaround.





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††See limited warranty & restrictions at dealer. Excludes normal maintenance & wear items.



is "an incredible five-year success story," says Gordon Johns, manager of the \$170 million Kemper Global Income Fund, 8% of which is invested in Finland.

But the Finns aren't just selling technology abroad. Finland is one of the most wired nations on earth, with more advanced-telecommunications networks and Internet users per capita than either the U.S. or Britain. Most companies have already switched from traditional local-area networks to new broadband networks geared to carry voice, data,

## Special Report

and video. Corporate multimedia services also are taking off.

In some ways, it's not mysterious that advanced telecommunications have flourished in this remote northern land. In the late 19th century, Finns developed hundreds of local phone companies to guard against interference by Russian czars who controlled Finnish territory. Although they still enjoy a monopoly over local phone service, 47 local phone companies banded together to challenge state-owned Telecom Finland's monopoly on long distance in 1994. Within four days after they were allowed to compete, they seized 60% of the market. Finland's phone rates are now among the world's lowest.

**MULTIMEDIA.** Finland also boasts the most advanced telecommunications infrastructure anywhere. Using asynchronous transfer mode (ATM) technology—a new standard for combining video, voice, and data—networks can transfer information 15 times faster than traditional local-area networks. Telecom Finland offers commercial multimedia services over its network at rates as low as a 10th of those in the U.S., Britain, and Europe.

Local startups are working hard to stay on the cutting edge. Three-year-old Oulu-based Elektrobit Ltd. pioneered the world's first entirely cellular office and is launching the first cellular pay phone. Perhaps most important, traditional industries have also undergone a technological overhaul. Even steel, paper, and pulp makers are churning out advanced electronics, from laser measuring devices to sensors and software.

Of course, in a place like Oulu, which has a population of just 100,000, there are some unusual twists. While the region's 4,000 engineers toil in sophisticated labs, most important decisions are made in the sauna. "It's like golf in other countries," says Pertti Huuskonen, president of Oulu Technopolis Ltd. It seems extreme cold, heat, darkness, and isolation can be powerful catalysts for innovation.

By Gail Edmondson in Helsinki

## BOMBAY

# 'Bollywood' Breaks Into the Big Time

**A**top a misty hill, rain falls, turning the heroine's sari into a clingy wrap. She lip-synchs to music while the hero, in a billowy shirt and tight pants, chases her playfully across the grass. They dance provocatively, and he clasps his arms about her. She slithers away.

Such a scene takes place in almost

from dubbed versions of such flag Western hits as *Jurassic Park* and *Speed*, Bollywood is rushing to enter the era of high-tech films. Producers are founding new companies, boosting their marketing, and seeking new sources of financing.

One of the key new players is A-

tabh Bachchan, a superstar actor during the 1980s, who launched a new film and entertainment company in May. Star cachet helped him pull in \$10 million from financial institutions—something no one in the Indian movie business had done before. Now, others are following. Bachchan's first steps, turning production and post-production houses into legitimate corporations.

**SOFTWARE.** Meanwhile, cameras are rolling for the first Bollywood high-tech films. CMM Ltd., a 18-month-old special-effects company backed by such giants as State Industries of India, has booked more than \$1 million worth of software and hardware from Silicon Graphics Inc., the Mountain View, Calif. computer company whose special-effects equipment is used by nearly every Hollywood studio. The technology is a key to a still-



every Indian movie. And there are a lot of them. With 800 produced a year, India churns out at least twice as many films as Hollywood, and revenues top \$1 billion a year. Yet India's Bombay-based movie business—nicknamed Bollywood—has long been known for schlocky films, an army of independent producers, and a barely functioning distribution system.

Now, Bollywood is undergoing a dramatic face-lift. Spurred by competition

**ACTION!**  
Cineplexes and high-tech effects are on the way

titled film featuring Indian megastar Rukh Khan in a double role, allowing him to appear with himself in the same scene. Silicon Graphics is lining up other clients in India as well.

To earn more money on its prod-

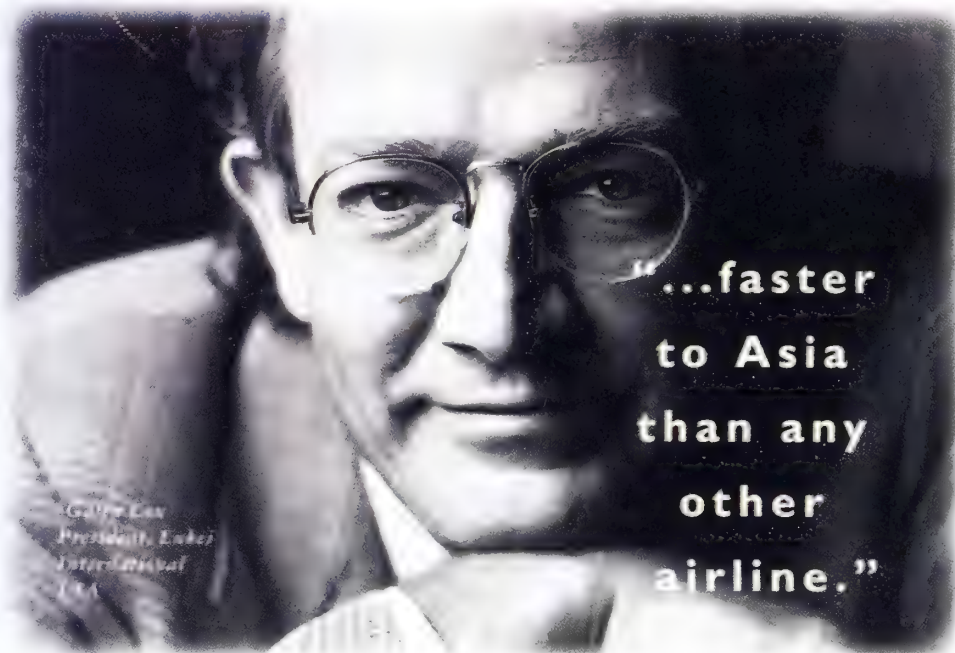
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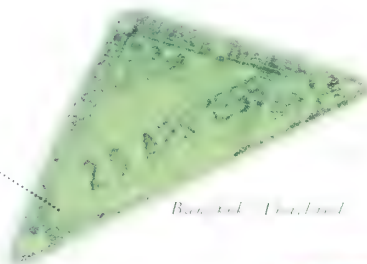
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*Beet, Vol. 1, No. 1*



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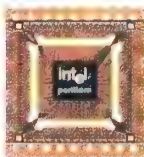


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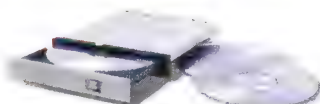
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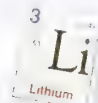
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wood is revamping its distribution. In the past, producers have sold films to a large number of distributors for a flat rate, sharply limiting income. Now, Modi Films—owned by an Indian conglomerate of the same name—is creating a distribution system that will provide producers with a share of the box-office take. The company is growing from its venture to distribute Bollywood films in India.

The first big success of the new Bollywood is *Who Am I to You?*, a musical that focuses on two weddings. Thanks to its traditional plot and effective marketing, it's India's biggest hit ever. Released nearly a year, the film has made more than \$30 million, a phenomenal amount in a country where the average moviegoer pays 65¢ admission and the average movie makes about \$3 million—barely what an art-house film makes in the U.S.

*Who Am I to You?* abstains from the violence of most Indian films. To

## INSIDE INDIA'S MOVIE BIZ

**BOX OFFICE OF A MOVIE \$1–2 million**

**BOX OFFICE OF A STAR**

**Up to \$1 million per film**

**BOX OFFICE OF A BOX OFFICE TAKE**

**Up to \$1 million per film**

DATA: BUSINESS WEEK ESTIMATES

attendance, the producers decided not to release it on videocassette. Many moviegoers have seen it three or four times. The producers also chose the best movie halls to show the film and had them specially decorated. Some producers even gave out flowers.

Audiences appreciated their efforts. More than 13,000 theaters have long been closed for their litter, broken seats, and muffled sound. But with the release of *Class of 1999* last year, "everything changed," says M.K. Ramakrishnan, a partner in R&S Electronics, Indian distributor for Dolby Laboratories Inc., which provides stereo sound systems to theaters. R&S has sold 50 Dolby systems and expects to nearly double that this year. Meanwhile, Modi Films, in a venture with United Artists Pictures Inc., is spending more than \$75 million to build 10-screen cineplexes in major cities.

As a result, movie audiences are on the rise after declining for a few years. The advent of cable TV. Foreign movies may be popular, but Bollywood is now grabbing at least 90% of the market. So along with lip-synched love stories, Indian audiences will soon see tech adventure and science-fiction too.

By Sharon Moshavi in New Delhi

## NEW YORK CITY

# Cyberspace on the Hudson

The digital gold rush is here. Suddenly, everyone from publishing and entertainment giants to advertising and music moguls are clamoring for new media—the audio, video, and graphical "content" for CD-ROM, film, and online.

That digital thirst is sparking a burst of creative activity across the country—in San Francisco, Seattle, and Austin, for starters. But nowhere is the ground as fertile as in New York. Hundreds of tiny companies started by artists, filmmakers, and musicians have sprouted up in the past two years—with names such as Razorfish, Pseudo, and Need 2 Know. These hopefuls join a handful of somewhat better-known pioneers, such as Voyager and Music Pen, seeking their fortunes in a gritty stretch of lower Manhattan known as Silicon Alley.

"EDGE." New York New Media Assn., formed a year ago to galvanize the new-media community, has seen its membership swell to 1,500 people representing 1,000 companies. Its monthly "cybersuds" get-togethers, once intimate affairs hosted in company offices, now regularly draw crowds of several hundred.

What brings these brave souls to New York, with its harsh rents, high taxes, and outdated buildings? "It has to do with edge, attitude, and proximity," says Jerry Michalski, managing editor of *Release 1.0*, a newsletter for the digerati.

**VIRTUAL IVORIES**  
Tin Pan Alley intersects with Silicon Alley at Music Pen

It also helps that New York is the traditional power base for publishing, entertainment, and advertising—the industries whose confluence powers new media. Virtually all of the media giants have new-media units, but most still look to smaller outfits for creative skills. "Whether you are a small company or an independent contractor, it behooves you to be

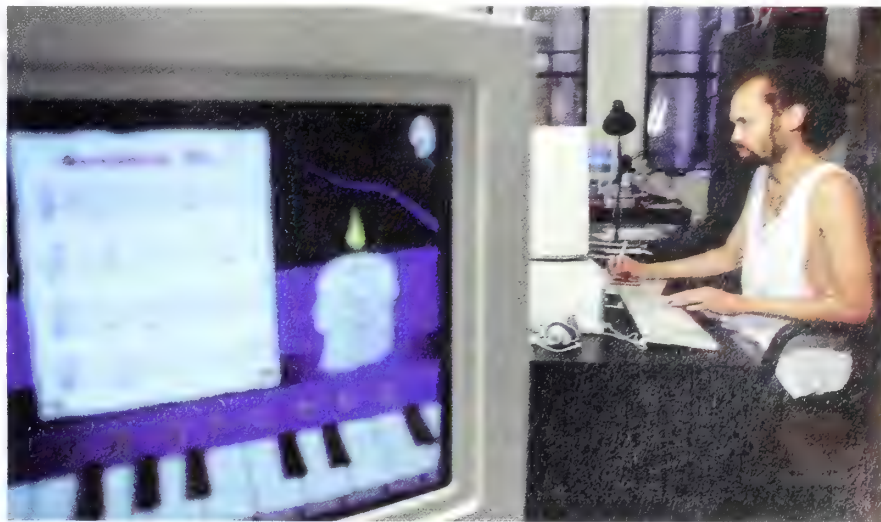
## Special Report

in New York," says Gene DeRose, president of Jupiter Communications Inc., a market researcher in Soho.

City planners are doing their part as well. Mayor Rudolph W. Giuliani has drafted a revitalization plan that offers a series of incentives, including deep tax cuts and energy-cost savings, to attract and retain small businesses in lower Manhattan. The state senate is expected to approve it at a special Oct. 11 session. Plus, a venture fund earmarked for new media has been set up by the city.

But the core of New York's efforts is the Information Technology Center, a 31-floor building equipped with high-speed fiber optics that will provide facilities for dozens of new-media companies when it opens this fall—in the former headquarters of Drexel Burnham Lambert Inc., the defunct icon of New York's go-go years. The symbolism isn't lost on the Center's city and corporate backers, who hope Silicon Alley will yield gold yet.

By Amy Cortese in New York







## SOWETO, SOUTH AFRICA

# Brisk Business in the Townships

It was highly symbolic: When the map of Johannesburg was redrawn, the black former township of Soweto was sketched in as part of the business center. Most whites have never ventured into the township—known for crime, squalor, and antiapartheid protests. Yet these days, white accountants, bankers, and retailers are swallowing their fears and heading in that direction.

The reason is simple: Soweto and other such townships are where the economic action will be in the new South

nevertheless suffers from a shortage of retail outlets. It's a magnet for new businesses because it's larger than any other township and the home of successful black politicians and entrepreneurs.

The most visible project so far is the township's first mall. Built for \$12.1 million by Sanlam Properties, one of South Africa's largest commercial developers, the Dobsonville Shopping Center mixes national retailers with nascent black enterprises: a hair salon and a bookstore, along with movie theaters, restaurants, and banks. Opened in September, 1994, Dobsonville is the test that "everyone is watching with four eyes," says Sanlam's regional property manager, Swani Swanipole. "Will it make money?"

The jury is still out. The center's white managers admit that their lack of understanding of black consumers' demands has caused glitches. Another problem is transportation: Few township dwellers have cars. People get around on private minibus taxis, but more routes go downtown than around Soweto's winding streets. So now, the retailers may set up a free bus service.

Despite these difficulties, the main store in the mall, a 23-checkout Shoprite, is doing brisk business. Soweto's first big supermarket, it consistently

## CHECK IT OUT

Investors are "watching with four eyes" to see how the new center fares

beats sales target by maintaining the same standards in white neighborhoods. Up till now, most Soweto residents bought groceries in downtown Johannesburg, where quality is better than in the small local shops. The Shoprite "is what we've been waiting for," says white customer Gilbert Nkosi, a weekly customer.

Now, city planners are drafting a long-term plan to integrate Soweto with central Johannesburg. They want to create a commercial, industrial, and residential corridor around Soweto's main Baragwanath Hospital. The National Business Initiative, a private-sector partnership with the government, is also working to ease investors' fears about building township infrastructure projects.

**PARTNERS.** For white businesses moving into Soweto, community leaders recommend hiring black managers and making a visible contribution to the neighborhood. "You must develop a partnership with the community—in that, you have protection for your investment," says Max Legodi, executive director of the Soweto Chamber of Commerce.

One example is Buildware Market, a construction-supply warehouse that opened recently in a new business center. Buildware is a joint venture between Murray & Roberts, a major construction company, and two black entrepreneurs, Ndaba Ntsele and Sibusiso Sithole. Instead of maintaining its own fleet of trucks, Buildware hires Soweto taxis with pickups to deliver its goods. A snack bar is run by local women, and pay telephones were installed to

## SOWETO AT A GLANCE

**POPULATION** Up to 4 million

**AVERAGE HOUSEHOLD SIZE** 5.2 people

**AVERAGE MONTHLY HOUSEHOLD INCOME** \$50

**SHOPPING MALLS** 1

**HOUSEHOLDS WITH RUNNING WATER** 78.4%

**HOUSEHOLDS WITH SEWAGE** 66.7%

DATA: BUSINESS WEEK ESTIMATES, URBAN DEVELOPMENT STUDIES

the mostly phoneless neighborhood.

Although jackhammers aren't sounding across Soweto, plans are circulating for casinos, more shopping centers, an industrial park, and a hotel. Sanlam may also put up an office building. Other developers "are jealous," says Sanlam's Swanipole, "because we've learned what they still have to learn. Soweto and other townships are markets they can't afford to ignore."

*By Drusilla Menaker in Johannesburg*

## Special Report

Africa. Demographers predict a rapid shift in spending power to the black majority, bolstered by better earnings now that apartheid has been lifted. The government is pushing new roads, water lines, and sewers and is offering housing subsidies in the townships. Says Brian Meyers, marketing director at Shoprite Checkers Ltd. supermarkets: "The central business districts and white suburban areas are not going to give us the kind of growth we need. We will have to move into the black areas."

Soweto is the first township to attract pioneering investors. With a population estimated at up to 4 million—there has never been a census—Soweto



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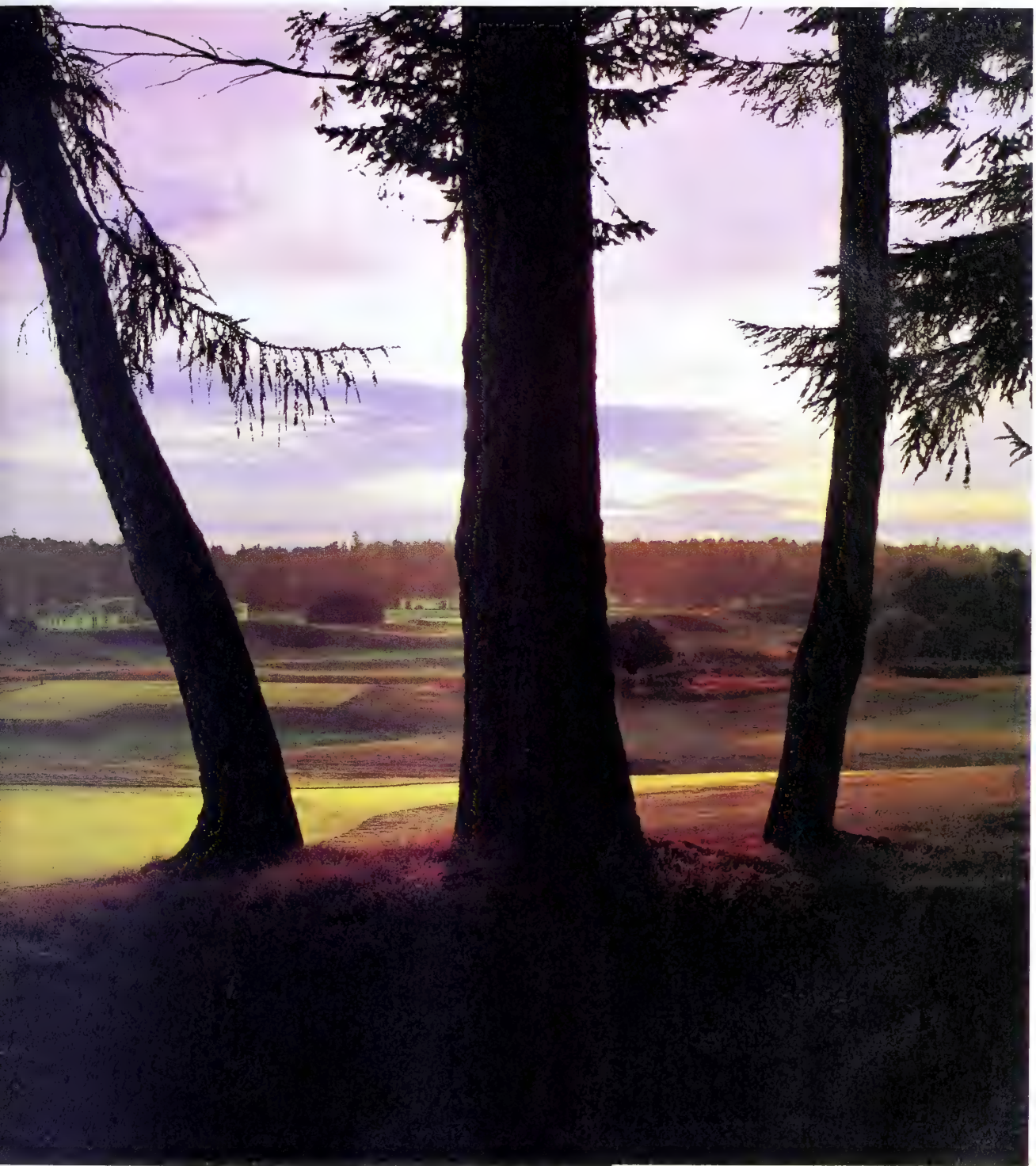
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# IS IN-HOUSE DESIGN ON THE WAY OUT?

Budgets are rising, but for outside firms and new technology

It's not *sex, lies, and videotape*, but the drama of CAD, cost, and cycle time that's generating a revolution in the business of design. Pressure to install computer-aided-design technology, cut project costs, and sharply reduce time to market for new products is revolutionizing in-house design departments, from IBM to Rubbermaid, from AT&T to Steelcase.

A new survey by BUSINESS WEEK and the Industrial Designers Society of America of 53 design departments in America's largest companies reveals that decentralization is in, budgets are up, staffing is down, high-tech spending is up, and time to market is down.

**HARD-WON RESPECT.** The survey, which asks corporate design managers to compare their business in 1990 to today, shows that after years of internecine warfare with marketing and engineering, design has finally won the respect of top management. "There is more recognition of the value that design brings to the product by the business side than ever before," says Lee Green, manager of corporate identity and design at IBM. "It's become a strategic tool."

The payoff is in rising design budgets, up by an average of 15% to 20% annually over the past five years. Some companies have seen even sharper hikes. Black & Decker Corp.'s

North American design budget rose from \$300,000 in 1990 to \$1 million this year.

One clear trend is that most of the dollars are going for high technology. Tech budgets are growing 50% to 100% a year, according to the survey. Many are three times what they were in 1990—some, five times. For designers, CAD literacy is now a prerequisite. The largest sums are going for software, with Pro-Engineer clearly becoming something of a national standard.

Another unmistakable trend: Money is not going to build bigger staffs. In fact, the majority of corporations are downsizing their central design departments like crazy. It's all part of the great decentralization of the American corporation. The need to get closer to customers and speed up the time from concept to finished product is pushing companies to get design out of headquarters and down into the basic business units. "We're committed to a '10X' [10 times] reduction in cycle time over the next two years," says Rudi Krolopp, director of industrial design at Motorola Inc. "We have to take design out to



## Back to the Drawing Board

How big corporations are managing design work

### DOWNSIZING

Staffs are being reduced or held constant while the workload is soaring.

### SPENDING

It's way up for computers, software, and other high-tech gear. Literacy in computer-assisted design is imperative.

### DECENTRALIZING

Design staffs are being dispersed to operating units to speed product development and time to market. Independent design shops are being brought in to team up with in-house groups to spark innovation and save money.

### TIME TO MARKET

The cycle time from concept to product is being cut to beat the competition and save on cost.

### RAPID PROTOTYPING

The hottest technique to speed up input on a new product from customers, suppliers, marketers, engineers.

where the products are made, to the operating units. My function is not corporate. You die if you're at the corporate level."

Decentralization is leading to a massive outsourcing of design work by large corporations. Independent business units are increasingly turning to outside design consultancies. Sometimes it's in conjunction with in-house company designers and sometimes not.

That is changing the entire function of

in-house corporate designers, who are and more are brokers for outside consultants. "Increasingly, designers in big corporations play two roles—internal champions for specific products and integrators who connect outside designer functions with inside functions," says Brian Vogel, chairman of the Design Management Group for the IDSA, a senior vice-president of Product Genesis, a design shop based in Cambridge, Mass. **LOCAL TIES.** Where are companies going to farm out design work? Not surprisingly, to designers who know the culture. Often, these are people who used to work for them and have gone out to launch their own companies. They

are the right software to connect with the parent company and can do more than is possible inside the company. They also tend to be around. In an era of globalization, the localization of design has become important.

The scope of outsourcing is staggering. In the BW/IDSA survey, one multibillion-dollar company said it outsourced "everything" needed to do product development. Another listed "model-making, prototyping, graphic development, computer services, market research, materials selection." Yet another corporation answered "full-service product development firms, small job shop, including illustration, mechanical engineering, human factors, and industrial design."

In response to customer demand, a growing number of independent design consultancies, such as IDEO, Product Genesis, offer everything from research and engineering to product development, pilot products. Design Edge in Austin, Tex., is even manufacturing computer screens for clients after it finishes signing them.

In-house designers for big corporations were once "design managers." Today, they manage not design per se, a multitude of designers.

By Bruce Nussbaum in New



# INSURANCE

## The Keystone of Financial Planning

by Stephen M. Pollan and Mark Levine

**T**here's no element of the financial services industry that suffers from a bigger gap between perception and reality than insurance.

Often maligned and criticized, insurance is actually a versatile tool providing essential stability to both individual lives and businesses. The industry, far from being boring, is visionary and creative, having flourished because of its ability to recognize the changing needs of society and create new products to meet those needs.

As a new century approaches, the insurance industry faces a wide range of challenges that demand greater service and new products for home and business. For the insurance consumer, whether an individual or a business, this means even more useful new tools to help smooth life's sometimes bumpy road.

### STRATEGIES FOR RETIREMENT INCOME

Retirement is a mixed bag of excitement and apprehension. The excitement comes from the freedom to do what you want. The apprehension comes from worrying about whether you'll have enough money to live out the rest of your life.

"One insurance product we recommend for retirement planning is the variable annuity," says Michael J. Chasnoff, a certified financial planner and president of Advance Capital Strategies, Inc. "These are mutual fund







accounts that have a life insurance component that allow the investment portion of the account to grow on a tax-deferred basis. You can contribute as much as you want, and they escape taxation until you begin to draw money out."

If an individual has a continuing life insurance need in addition to a retirement cash flow need, many brokers recommend variable universal life insurance. These policies combine a term insurance component with a savings component.

### STRATEGIES TO PAY FOR COLLEGE

With the best private colleges and universities rapidly zeroing in on the \$30,000 a year level, paying for college has many parents in a panic.

Peter Roselli, an insurance consultant with Press, Fishman, and Rappaport, says that life insurance policies offer advantages that other forms of college tuition directed investment do not. One is that a life policy creates an estate for the policyholder. Another advantage is the waiver premium most policies offer. If the policyholder

becomes disabled, the insurance company pays the premiums. "Also, taxes on the cash buildup in a life policy are deferred," he notes. "You can take out cash and not pay any taxes until you've taken out more than the total of the premiums you've paid in."

The key to using life insurance to pay for college, according to Roselli, is to purchase a policy — either whole life, universal life, or variable life — when your kids are very young. "It takes ten years for a life insurance policy to be competitive with other forms of investment."

### STRATEGIES FOR LONG-TERM CARE

There's good news and bad news on the geriatric front. The good news is we're living longer. The bad news is it's expensive. For many families, long-term care insurance can help take the sting out of paying bills which could run as high as \$90,000 per year.

Jerie Charnow, owner of Charnow Associates, Inc., a consultation and care management service for older adults and their families, says "because more and more long-term care policies are

### TAKING THE PAPERWORK OUT OF INSURANCE BUYING

For the small business owner, competitiveness and the advent of new technologies are making buying insurance quicker, easier, and more efficient than ever before.

To market a new small business insurance product it recently created General Accident Insurance in Philadelphia is using an innovative on-line service that takes the paperwork out of the buying process, according to Jack Doyle, senior vice-president.

Using Sapiens International's Rapid Application Technology and the input of agents and customer service representatives, the company has created a system that allows the agent and customer to sit down at a computer and select from a menu of coverages. As the customer makes decisions about his or her needs, the agent enters the information into the system. It's then immediately transferred to GAI's mainframe at its corporate headquarters.

"Our system makes selecting coverages easy and efficient," says Dave Sagaser, also a vice-president with GAI. "We've built our underwriting criteria right into the system. This puts the processing power in the agent's office and lets customers select the type of coverage they want, the amount of coverage, and their deductibles. As they look at different coverages, the quotes are right there in front of them. When they've finished, the information is loaded right into our system."



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being sold, the policies are getting better and the premiums are coming down." She says that benefits distribution also is improving. In the past, most long-term care coverage operated on a reimbursement system. Many of today's policies give the policyholder much greater latitude in spending. Finally, Charnow says that state and federal initiatives are underway that will make long-term health care premiums either tax deductible or qualify them as a tax credit.

"I'd say if you're over 50, it's time to start looking," says Charnow. "Nearly one-third of the people receiving long-term care benefits in this country are under the age of 55. Also, the sooner you buy it, the cheaper the rates. And they usually don't go up."

### STRATEGIES TO MAINTAIN A THREATENED INCOME

We all run the risk of a sickness, disability, or terminal illness that could threaten our jobs, our income, and our savings.

"Protecting a stream of income is one of the basic values of insurance," says Madeline I. Noveck, a certified financial planner and president of Novos Planning Associates, Inc. Everyone needs health coverage, and many people are covered through their employers. For the self-employed, both personal plans and group plans are available in the market.

"And most people should get disability coverage as soon as they begin working, even before a life policy," recommends Noveck. "Statistically, the likelihood of a short-term disability is much higher than an unexpected death. So unless a person has other resources to fall back on, disability insurance is critical."

For a person with partial disability coverage paid entirely by their employer, supplemental coverage can often be purchased. "Many supplementary coverages are quite affordable because of the long waiting period before they go into effect," says Noveck. "But you have to be careful to make sure the policy is clear on when the benefit becomes payable."



Adult-care specialist Charnow says that for the terminally ill, the accelerated death benefits of a life insurance policy can be a source of needed income, as can a loan against the policy's cash value. Selling life policies for prices below their face value is also becoming common, particularly among AIDS patients.

### STRATEGIES TO MINIMIZE TAXES

Keeping the tax man at bay is of interest to everyone, particularly when money intended for our spouse or children is involved.

Bruce Pritikin, an attorney and CPA with Robbins, Pilman, Slayton, and Halfon, says "If we're focusing on providing for the loss of the bread-

winner's income, we recommend the purchase of a term life insurance policy. The proceeds are exempt from estate and income taxes and the surviving spouse enjoys the full benefit of the policy."

Other products with tax benefits include adjustable and whole life policies, which allow the policyholder to take cash value of the policy without tax liability (as long as the amount taken out remains below the total premium that has been paid in over the years), and variable annuities that have life insurance components that provide tax-free death benefits to spouses. Another strategy is to establish a life insurance trust, which allows the death benefit to be excluded from the insured person's estate.

For couples whose goal is to provide for their children, second-to-die insurance, in which the benefit is not paid until the surviving spouse passes away, can be a useful product. "It's also a useful tool to cover estate taxes due upon the death of the second person," says Pritikin.

Finally, the way a life insurance policy is purchased can have tax advantages. If an individual belongs to a pension plan that allows investment in life insurance, the premiums are tax deductible.

### BUSINESS INTERRUPTION INSURANCE

When the Federal Building in Oklahoma City was bombed last April, undoubtedly lost behind the tragedy of the people killed was the story of the dozens of businesses forced to close as a result of the incredible damage the bomb caused in surrounding blocks. For many, ownership of a business interruption policy was probably the difference between reopening and finding another line of work.





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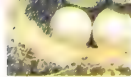
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"Business interruption insurance responds when a business is in peril due to an unforeseen and uncontrollable event like a fire or windstorm or explosion," says Bob Murphy, senior vice-president with Alexander & Alexander Services, Inc. "The policy covers the loss of income due to the interruption and stays in effect until the business is able to start up again."

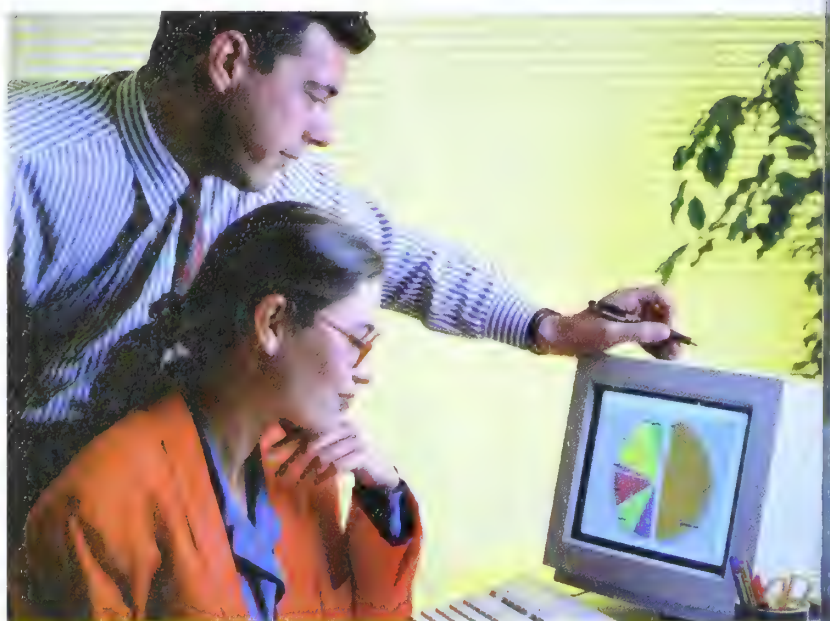
Since there are a wide variety of events that can interrupt a business, there are a number of specialized business interruption coverages that can be tailored to meet the specific needs of the client. "There's really no risk that can't be covered with the proper premiums and deductibles," says Murphy.

#### KEY PERSON INSURANCE

Here's the situation: You have an expensive, technically-complex product that has taken off and is rapidly seizing market share. As a result, your company is booming. But the real knowledge of the product rests with just one individual in the company. If that person should die or become severely disabled, the business could be in serious trouble.

"Key person insurance is an important tool for any company whose bottom line can be jeopardized by the loss of an individual," says Jesse Gottlieb, also a senior vice-president with Alexander & Alexander. Key person coverage is important in helping a company maintain the confidence of its other employees, its customers, and its creditors. "This is frequently a big concern of small companies, where there is seldom enough depth of talent to provide a replacement from within. It buys the company some time to get back on its feet."

Key person insurance is actually a life insurance policy with the company



named as beneficiary. Although the premiums aren't tax deductible, the proceeds are almost always exempt from income tax. The benefits can be used to recruit and train a person to serve as the key person's replacement and recoup profits lost because of the person's death.

#### PROTECTION AGAINST BAD DEBTS

Every year, thousands of businesses fail in the United States. Each has a list of creditors who, unless protected by credit insurance, are lucky to get a few pennies on each dollar they're owed.

"A customer's bankruptcy can be catastrophic and is rarely predictable," says Frank Reo, another vice-president of Alexander & Alexander. "Credit insurance can protect them against the insolvency of customers."

For businesses going global, export credit insurance is increasingly popular. In addition to covering policyholders for their customers' insolvency, it also covers for losses caused by default as well as those caused by political events. "It's a good tool for the

business person who might otherwise be timid about exploring the global marketplace," says Reo.

An even more specialized product — political risk insurance — is available for companies doing business in emerging nations whose governments may be somewhat shaky.

#### PROTECTION AGAINST LIABILITY

We live in an increasingly litigious society. As a result, one of the biggest challenges facing insurance companies in the last decade has been the upsurge in lawsuits against their policyholders and the enormous awards collected by plaintiffs.

For many businesses, protection against liability suits related to products is a primary concern. For the professional, protection against malpractice suits is the goal, as it is with hospitals and other service providers. The requisite coverage is readily available, and at virtually unlimited quantities.

"In terms of coverage the sky's the limit," says Alexander & Alexander's Bob Murphy. "Some companies have

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hundreds of millions of dollars in excess liability insurance. It depends on their business and how much comfort the board of directors wants.”

Most companies and professionals acquire liability insurance in layers. The cost of the first layer, called ‘down and dirty’ in the industry—is determined by the type of product a company

manufactures or the type of work a professional is involved in. Additional levels, or attachment points, can be added to increase coverage for more remote exposures, allowing a company to keep building protection layer by layer in a cost-efficient manner.

Offering such an innovative solution to simultaneously rising costs and

needs is a prime example of what allowed insurance to remain a vibrant and profitable service. From its beginnings nearly 3000 years ago, to its modern day responses to emerging risks, the insurance industry has always had the vision to spot new dangers and the creativity to develop fresh ways of mitigating them. ■

## A BRIEF HISTORY OF INSURANCE

As far back as 900 B.C., traders on the island of Rhodes in the Aegean Sea were insuring themselves against maritime disasters by joining together to share the risks of their profitable yet dangerous enterprise. By the Middle Ages, Italy was the hub of European trade, and Italian shippers dominated the seas. Fragmentary historical records indicate early forms of commercial insurance were developed in Florence and Venice as far back as the early thirteenth century. The practice later expanded to London, Antwerp, Amsterdam, and eventually the United States.

### Fire Insurance

In 1666, the Great Fire of London destroyed more than 13,000 houses and tragically demonstrated the need for a formal shared risk against losses due to fire. By the early eighteenth century, fire insurance companies were common in London and were conducting business as far away as Wales and Scotland.

The earliest known fire insurance offered in America was provided in 1735 by the Friendly Society for the Mutual Insuring of Houses Against Fire in Charleston, South Carolina. In Philadelphia in 1736, Ben Franklin organized the city's first fire insurance company, the Philadelphia Contributorship for the Insurance of Houses from Loss by Fire.

### Life Insurance

In ancient Rome, citizens from the lower classes formed “collegia,” associations to which they regularly contributed a nominal sum and from which they could draw burial expenses when a family member passed away. In the Middle Ages, the populations of many European villages or towns agreed to share in the burial costs of residents, insuring individual families would not have to bear the costs by themselves.

By the seventeenth century, life insurance was becoming a more sophisticated strategy for providing financial security. The primary reason was the advent of statistics. Mathematicians began to develop mortality tables to which insurance rates could be linked.

In 1759, the Presbyterians founded the first life insurance company in the American colonies, the Presbyterian Ministers Fund. The Episcopalians soon followed suit.

By the mid-nineteenth century many of today's biggest insurance companies had been formed. Mutual of New York, New York Life, Aetna Life, Massachusetts Mutual and several others were all founded between 1840 and 1851.

## Industrialization and Development in the Twentieth Century

Between 1850 and 1900, new trends in the workplace resulted in the development of accident and health insurance, bond insurance, and fidelity and surety bonds.

In 1898, the first automobile policy had been issued to a physician from Buffalo, New York. Wilbur and Orville Wright had scarcely finished their epochal 1903 flight at Kitty Hawk, North Carolina, when the need for aviation insurance became apparent.

In 1910, the first workers compensation law was enacted to protect the well-being of injured workers, and many companies began offering the new form of insurance. In 1911, another new idea—group insurance—was developed to provide blanket coverage for the entire work force of a company.





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EDITED BY OTIS PORT

## NOW, 'GUNSIGHTS' FOR GENE THERAPY'S MAGIC BULLETS

IN THE FIVE YEARS SINCE DOCTORS BEGAN testing gene therapy, the results have been disappointing. It's easy enough to arm cells with a therapeutic gene and inject them into patients so that the doctored cells will secrete a beneficial product—say, a certain enzyme—into the bloodstream. But it's hard to get sufficient quantities of the enzyme to the sites where it's needed. To date, there have been no cases where gene therapy has definitively saved lives.

Inder Verma, co-director of the Salk Institute's Laboratory of Genetics in La Jolla, Calif., says there may be a better

delivery system. Described in the August *Proceedings of the National Academy of Science*, it combines a harmless mouse virus with an antibody that will bind only to receptors in liver cells. Give the virus an altered gene, expose it to liver cells in vitro, and it binds to the correct receptor and passes along the gene.

In principle, such an approach could deliver a variety of medications, including clotting factor for hemophiliacs. And by pairing the virus with different antibodies, Verma believes he can target any organ in the body. Human tests could be three to five years away.

## THERE'S OIL NEAR THEM THAR WELLS

THE ENERGY DEPT. FIGURES the U.S. still has twice as much oil underground as has been extracted. Much of it is even near existing wells. But until recently, the best way to find it was to drill a fresh hole, an expensive and environmentally destructive task. Now, Paramagnetic Logging Inc. in Palo Alto, Calif., is licensing a system that can prospect for overlooked deposits by looking through the half-inch-thick steel casings that line existing oil wells.

The key: Rock contain-

ing oil and gas resists an electrical current much more than rock that has been saturated with the salt water used to squeeze out oil. So PML's equipment runs a current from electrodes deep in the well to electrodes on the

surface. Engineers spot oil deposits by carefully measuring how much current leaks through the steel into the surrounding rock—using sensors that can detect changes as minute as a billionth of a volt, even when under intense heat and pressure. Oil-field giant Schlumberger Ltd. patented a similar concept four decades ago but lacked today's ultrasensitive micro-components. Schlumberger has licensed PML's system, which was developed with support from the Gas Research Institute in Chicago and the Energy Dept. It has won high marks from companies such as Arco and Mobil Oil.



## GRAY'S FEET OF CLAY

CRAY RESEARCH INC. HAS always reigned as the champion of supercomputers. But momentous changes are sweeping the supercomputing community, according to surveys by Jack J. Dongarra, a senior scientist at Oak Ridge National Laboratory. Silicon Graphics Inc., a no-show among the world's top 500 supercomputing sites in early 1994, now has more

high-performance installations than Cray—128 to 125. Cray Research is still far ahead in total installed computing power. But Larry L. Smarr, head of the National Center for Supercomputing Applications at the University of Illinois, predicts that even the knot-tiest problems will soon be tackled with linked clusters of computers built with the same "brain" chips used in

desktops. Even Cray has unveiled such a machine.

Moreover, by late next year, the fastest traditional super will be choking on the dust of the first "teraflops" computer. That's computerese for crunching an incredible 1 trillion calculations every second. Computer makers have been racing for a decade to break the teraflops barrier.

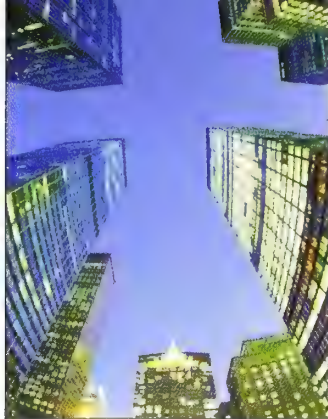
And the winner? Intel Corp. The chipmaker has just been tapped by the

Energy Dept. to construct a \$46 million, 1.8 teraflop machine for Sandia National Laboratories. No surprise, really. The current speed record—281 gigaflops—was set last December at Sandia by a linked pair of Intel supercomputers that share 6,768 microprocessors. To reach teraflops speeds, the new supercomputer will have 9,000 of Intel's next-generation P6 chips, scheduled to leapfrog the Pentium later this year.



## INNOVATIONS

■ If you stumble into a cafe at dawn, and your flapjacks arrive with "Good Morning" baked into the top, look for a robot called Flip-It. Developed by Ernesto Blanco, an engineering professor at Massachusetts Institute of Technology, Flip-It dispenses breakfast, cooks one side in an embossed fry pan, covers it with another, and turns both sides over. Flip-It is so foolproof it can be installed in cafes as a coin-operated system. ■ Evidence from the University of Georgia and Washington University's School of Medicine suggests that thermal equipment can treat the HIV virus. The heat-sterilization methods used in Latin America and Europe produce this. But in some developed countries, dentists get chemical sterilization, which may not kill all the HIV trapped in machine lubricants.



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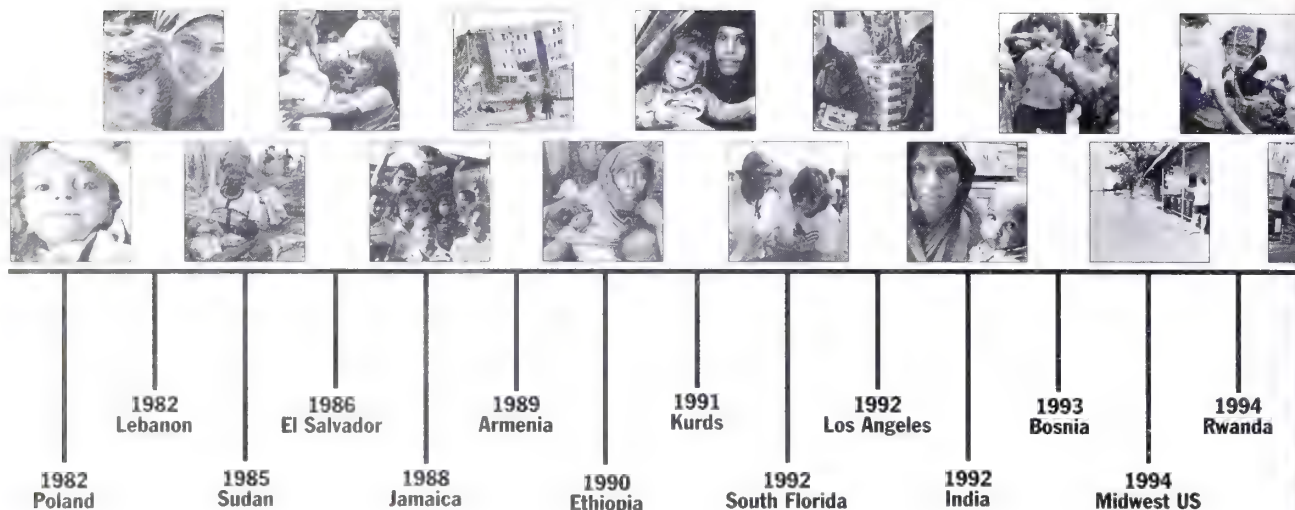
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\*Please call before 6:00 p.m. to cancel your Assured Reservation and avoid being billed for the first night.

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**140A-CA**



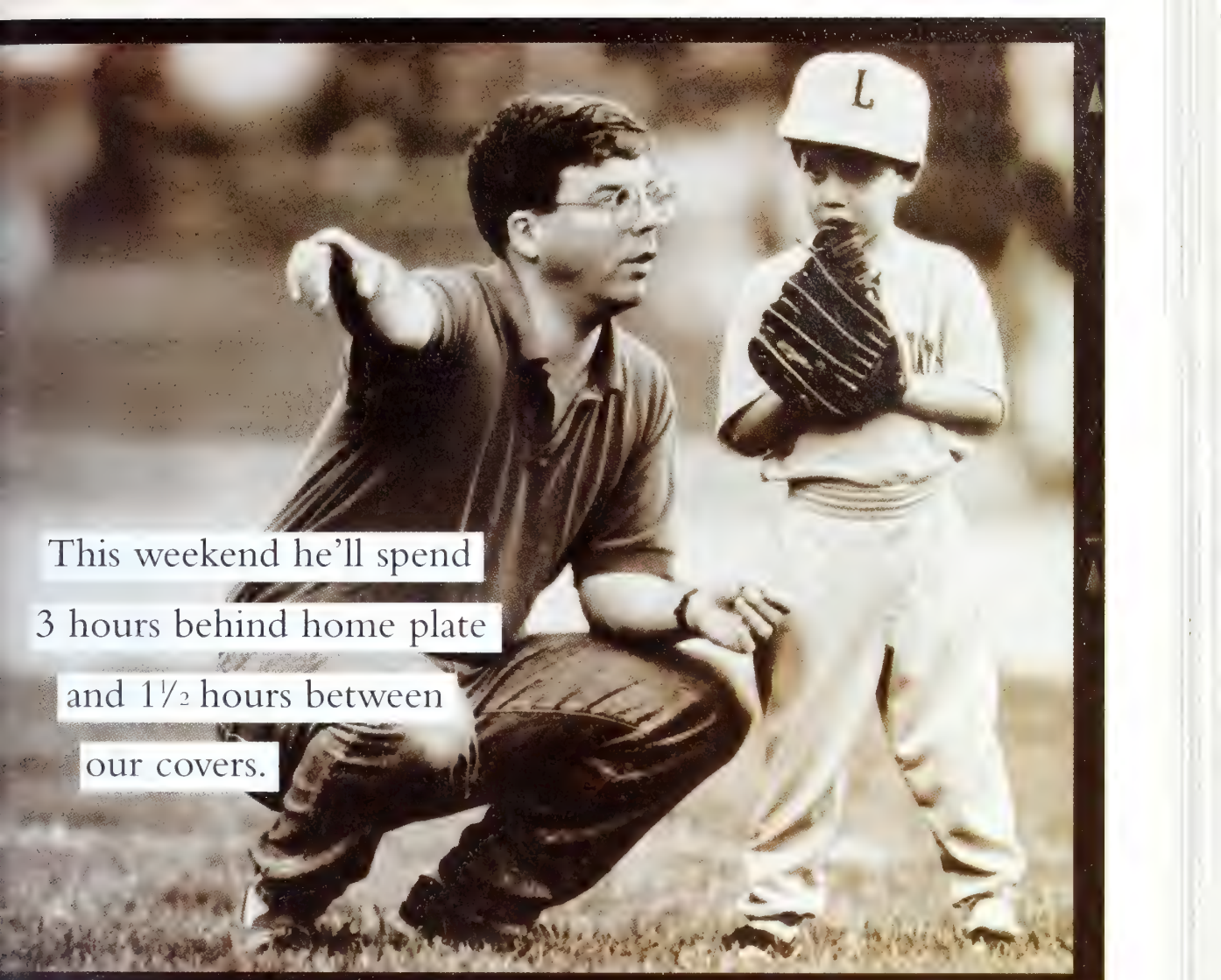


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■ It seems whenever and wherever there's been a need in the world, AmeriCares has been there. Speeding food and medicine to the tent cities, the refugee camps, the makeshift hospitals where people go to escape death. And sometimes, luckily, do. ■ AmeriCares ignores politics, caring only for the victims. So we're most often first in to areas of suffering. First with relief. First with hope. ■ We've discovered that help differs from disaster to disaster. For Rwanda and Sudan, it's food and medicine. For Bosnian refugees, it's also wool to make clothes to stay warm. In south Florida, AmeriCares Home Depot delivered construction materials to rebuild shattered homes – and lives. ■ AmeriCares figures out what's needed, goes to corporations for contributions of their products, and gets them where they have to be. ■ Creative, caring solutions are as varied as the crises facing the world. ■ But chartering planes, or buying jet fuel, doesn't come cheap; then again, neither does life. ■ Please help by sending your tax-deductible donation to AmeriCares, 161 Cherry Street, New Canaan, Connecticut 06840. Or call 1-800-486-1818. ■ People live because AmeriCares.

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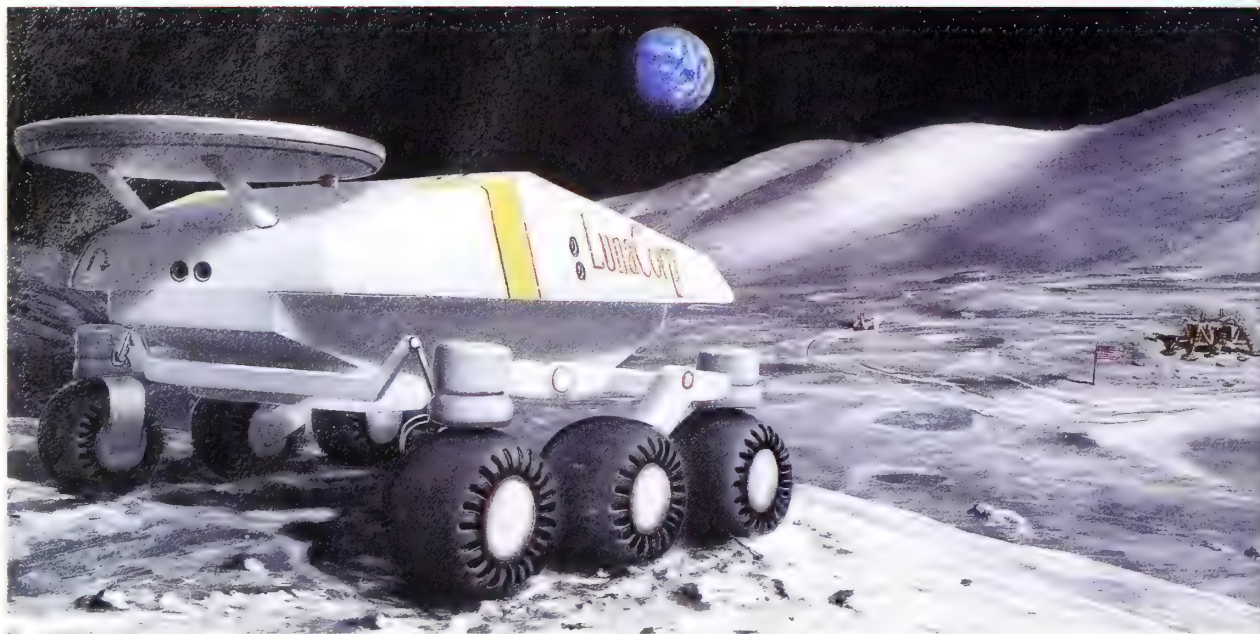
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## SPACE

# IS THERE MONEY ON THE MOON?

LunaCorp wants to send the first private mission

A year ago, while a tarantula-like robot called Dante II inched its way down an Alaskan volcano, scientists at Carnegie Mellon University were amazed by the attention that ensued. Dante became a media darling, and its stumble in the volcano and helicopter rescue even added a touch of pathos. "Dante had a half-million hits on its Web page" during its two-week saga, recalls William L. "Red" Whittaker, director of CMU's Field Robotics Center.

All that exposure—and no paying customers. In today's information economy, where on-air minutes are buckets of gold, the NASA-sponsored Dante failed to cash in. The lesson wasn't lost on David P. Gump, president of LunaCorp, an Arlington (Va.) startup. Gump wants to send a pair of Dante's offspring to the moon and cover the \$150 million cost with information fees—from network exclusives to live video feeds into theme parks. It's time, Gump says, to "bring back some of the magic" of space.

If LunaCorp can raise the funds, the first private moon mission will be a glitzy event, with corporate customers paying

for each bit of data the six-wheeled robots send back. LunaCorp proposes to launch two rovers in 1998, probably on a Russian rocket. Powered by solar energy, the tele-operated vehicles would ramble 1,000 kilometers across the moon, sending back high-quality video images for two years or more. The signals would feed into a command center at a U.S. amusement park, where thrill-seekers would remotely steer the vehicles across the lunar landscape, seeing what the rovers see and feeling

a simulation of the jostling ride.

Gump isn't the only earthling with designs on the moon. The Japanese and Europeans also plan manned missions—in 1998 and 2001, respectively (table). Longer term, they hope to set up lunar colonies and for a helium isotope, He3, that could fuel a future generation of fusion reactors. But Gump wants quicker results. In 1974, he has devoted his life to outer space. The onetime publisher of space magazines now markets space-related products—such as his 1993 *Return to the Moon*, which has sold 24,000 copies. **NIKE MISSILES?** Turning the moon into a giant Luna Park is only part of Gump's scheme. He envisions soda-pop commercials beaming down. Shoe companies will pay for lunar footprints, he predicts, and networks will bid for live feeds as the rovers approach famous sites, such as the Apollo 11 landing sites. Many NASA scientists are cheering

**MOON BUZZ TO GO WHEN NO THEMES PARK HAS GONE BEYOND**

## Back to the Moon

### COMPANY NAME

LUNACORP

### PLAN

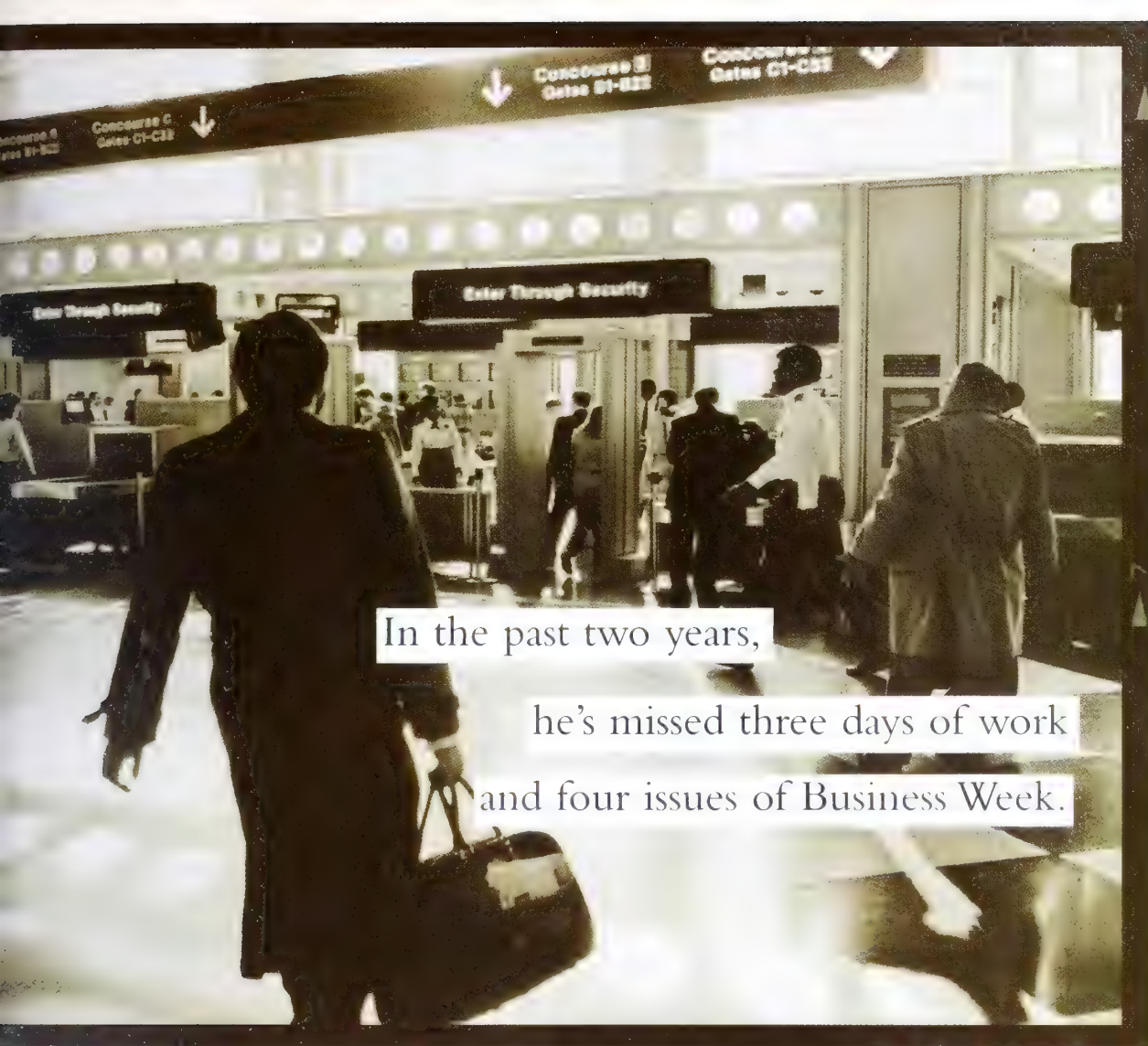
Launch two tele-operated rovers in 1998. Explore 1,000 km of lunar terrain over at least two years, sending back commercial video to theme park, television

JAPANESE NATIONAL SPACE AGENCY

Launch "penetrator" in 1998. Use probes to dig beneath the lunar surface to study chemical composition of soil

EUROPEAN SPACE AGENCY

Send rover to south pole of moon in 2002. Operate rover for first lunar days; survey surface, soil



In the past two years,  
he's missed three days of work  
and four issues of Business Week.

As professionals and managers, Business Week readers face tremendous demands on their time. Yet, 74% of them find the time to read every issue, every week. And nearly half of them read the magazine the day it arrives.

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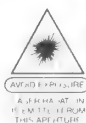
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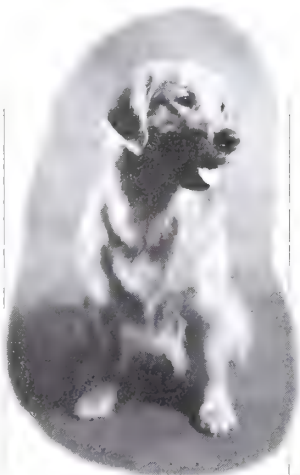
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## NATIONAL CENTER FOR FAMILY LITERACY

One in five American adults cannot read well enough to understand this ad.

That's why the National Center for Family Literacy is currently behind literacy programs for families in



Suite 200-B, 325 West Main Street, Louisville, Kentucky 40202-4251, for information on how to support family literacy. Or call (502) 584-1133 ext. 33.

If we, as a nation, can

**To 12 million adults this is an ad about a dog.  
Actually, it's an ad about literacy.**

over 1,000 communities across America. But there is much more we need to do.

We urge you to write the National Center for Family Literacy, Waterfront Plaza,

achieve full literacy, then we can achieve anything.



on, albeit from a distance. They in LunaCorp success will give the industry a boost. "It pioneers the says David Lavery, a NASA manager.

Gump has attracted a high-powered if unpaid—team. It includes Charles Thomas F. Rogers, a former Massachusetts Institute of Technology physicist who, while at the Pentagon, designed the first satellite communication system, and Mercury astronaut Scott Carpenter, an adviser. And "Red" Werner has already built robots to explore some nasty environments, including Three Mile Island nuclear reactor.

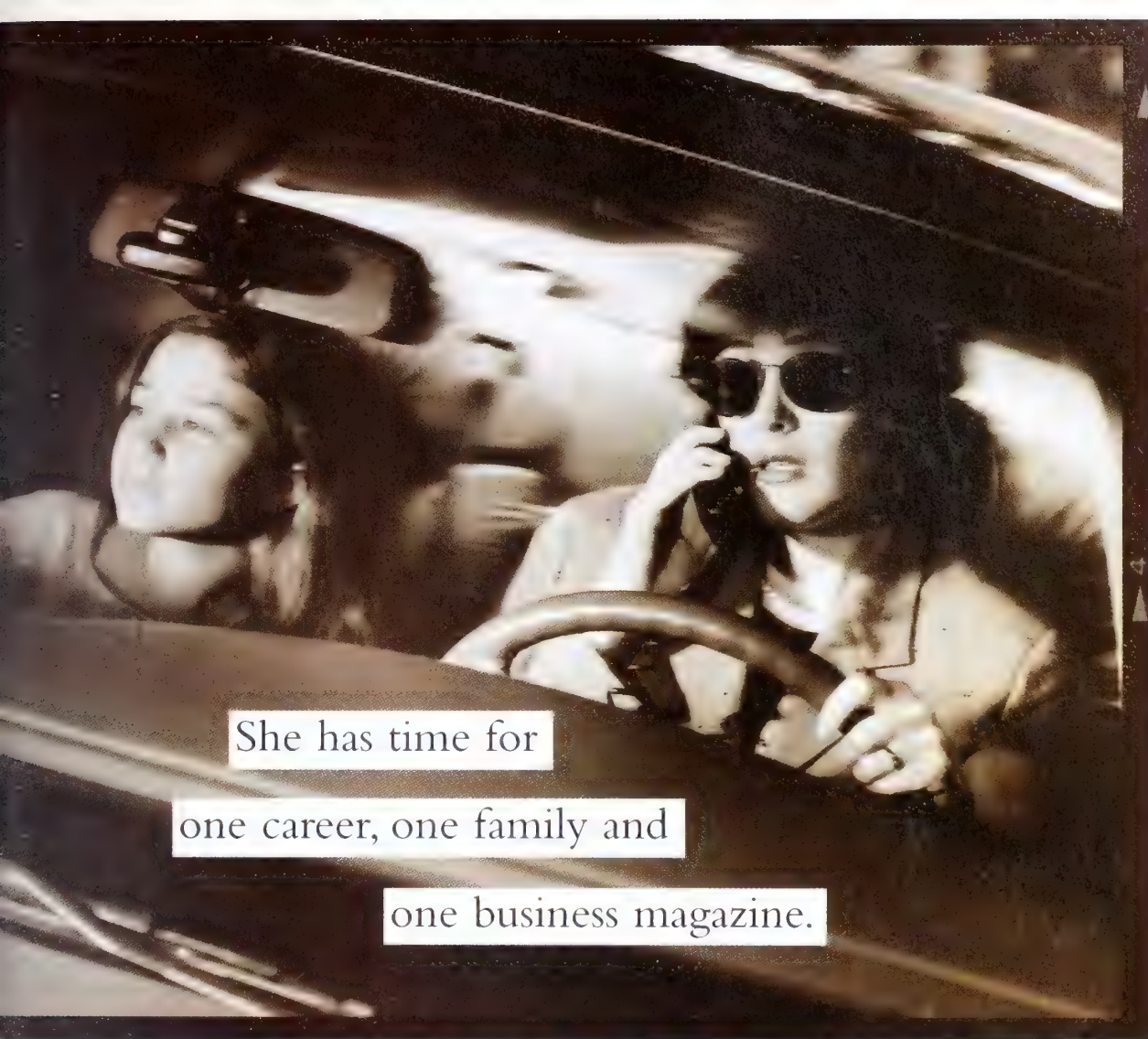
Turning the dream into reality cost \$80 million for the launch and a million for four rovers. (Two were spares, in case the first launch failed. The linchpin, Gump says, will be building a theme park for a \$40 million investment in a command center. He is in talks with Six Flags Corp. and Universal Studios but nothing is signed yet. Also in the mix is a convert—David Kennard, executive director of Information Design Associates, a unit of Foote, Cone & Belding. He has made presentations to Congress where the project is under "active consideration."

In contrast to financing, the technical challenges should be relatively easy. The prototype has already maneuvered a 100-km obstacle course in Pittsburgh. Next summer, it will head out on a 1,000-km desert jaunt. Making the robots smart enough to ignore destructive commands could take some time, though. Says Carnegie Mellon researcher Eric Krotkof: "We pretend the user who's malicious, who keeps trying to steer them over a cliff."

**NEXT STOP, MARS?** Perhaps the greatest hurdle is energy. The two-wheeled "day" provides plenty of solar power. But if the theme park demands continuous shows, the robots will have to perform during the lunar night, when temperatures plummet to 170C below zero. While nuclear power is one solution, more politically correct option is krypton gas, which produces heat as it radioactively decays. But krypton is expensive and could add \$50 million to the cost.

NASA has poured \$1.3 million into CMU's robotic research with hopes that similar rovers will eventually explore Mars. Could the Red Planet become a target for private enterprise, too? Perhaps, Gump says. It will take time for a new generation of space enthusiasts, investors will be much more eager to reach for their wallets once someone has made a buck on the moon—even if it's from sneaker ads and theme parks.

By Stephen Baker in Pittsburgh



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one career, one family and  
one business magazine.

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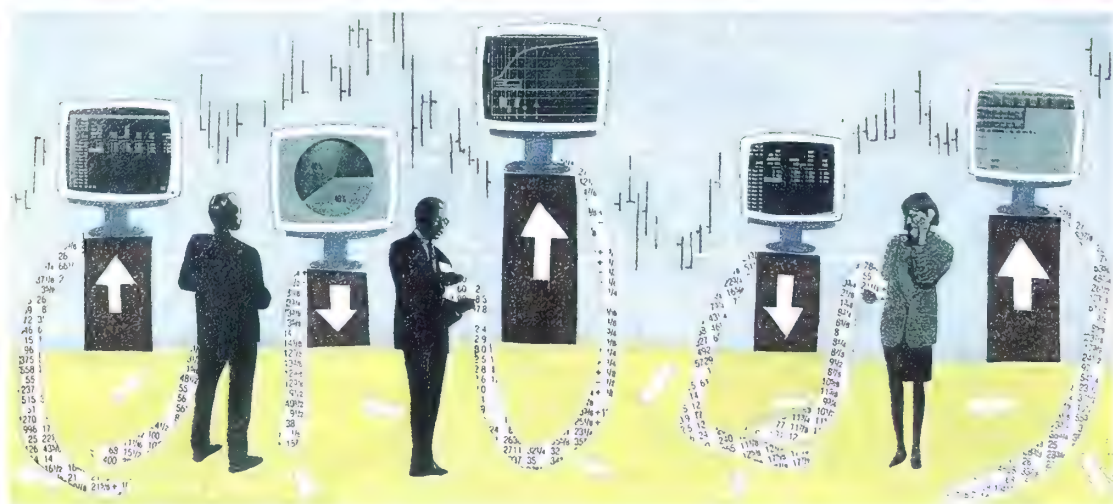
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EDITED BY AMY DUNKIN

## THE QUANTS MAY HAVE YOUR NUMBERS

If you invest in mutual funds, your portfolio is probably, at least in part, managed by machine. Many managers use computers to screen through thousands of stocks, allowing them to focus only on those with the best prospects. "It is mandatory to have some method of sorting through the massive information flow," says Thomas Madden, who oversees domestic equity investing at Federated Investors.

But a growing subset of managers known as "quants" are granting the computer a more active role in stock selection. It's hard to generalize about quant funds. Many are new, their methodology is complex and often secret, and their goals are diverse. With the stock market hovering near an all-time high, having a dispassionate computer assisting with buy and sell decisions might be comforting. And lately many quant funds are turning in impressive results.

Vanguard Quantitative, which seeks to mimic the

characteristics of the Standard & Poor's 500-stock index while outperforming it, has returned an average 12.34% for the past five years, while Vanguard's plain

vanilla S&P index fund has averaged an 11.9% five-year return. Quantitative Numeric, a small-cap fund recently closed to new investors, just earned a five-star Morningstar Inc. ranking, thanks to a 31% three-year average annual return. And Brad Lewis, who runs several quant funds to-

taling \$4 billion in assets for Fidelity Investments, is positively gloating over his new "black box" model, which has helped him rack up year-to-date returns of over 31% on his Stock Selector and Small-Cap portfolios.

"I don't think there is enough evidence to conclude that quant investing is always better than traditional research," says Amy Arnott, senior editor at fund-rater Morningstar. "But it's going to become more and more popular." Assets are flowing into many of these funds, and

new ones springing up. Quantitative Funds in Inc. Mass., has added three new funds in the past year. The most successful quant funds are in domestic equity. If you already have a U.S. stock portfolio, adding one to enhance your "Diversification" styles is important for investors like Lewis.

Unless you have a penchant for a somewhat eerie realm of computer science called artificial intelligence, you probably don't want to know the details of how these models work. Suffice it to say that the quants turn their investment theories into computer models, mostly using these fundamental measures of economic data that traditional managers do. But quants take into account complex relationships between factors and do analysis much more often and dispassionately than traditional spreadsheet analysts ever could.

**"OUR INSIGHTS."** Instead of looking at a handful of variables, such as cash flow, earnings growth, and price-to-earnings ratios, quant managers can program the computer to review 30 or 40 variables. Managers are constantly tinkering with their models, updating them as they fill

### Funds that Take Their Cues from Computers

| FUND                             | STRATEGY                                                                                                                                    | 3-YEAR TOTAL RETURN* |
|----------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|----------------------|
| <b>FIDELITY STOCK SELECTOR</b>   | Complex mathematical "black box" crunches reams of data and spits out lists of stocks with aggressive growth prospects at fair values.      | 161%                 |
| <b>QUANTITATIVE NUMERIC</b>      | Model sorts data on small-cap stocks every 30 seconds, looking for value and rising earnings estimates. Turnover rate is 350% a year.       | 390%                 |
| <b>VANGUARD QUANTITATIVE</b>     | Fund seeks sector weightings and risk characteristics of the S&P 500, but better performance. Computer runs 3,500 stocks through 30 models. | 100%                 |
| <b>VISTA GROWTH &amp; INCOME</b> | Seeking value plays, managers run a model monthly, narrowing down a list of 2,500 stocks, then following up with fundamental research.      | 170%                 |

\* Average annualized total return through Aug. 31, 1995

DATA: COMPANIES, MORNINGSTAR

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## BEEP IF YOUR PAGER SENDS VOICE MAIL

The trusty pager is about to get a makeover. This fall, the nation's major paging companies will begin rolling out a new generation of belt-buckling units that not only receive but also send messages. Some pagers will become mini-answering machines, capable of relaying voice messages, rather than



just phone numbers and a few lines of text.

These sophisticated services are possible because the federal government began auctioning off new space on the airwaves a year ago. More than a dozen paging companies bid \$600 million for access to that space and are now expanding services to utilize the frequencies.

**CELLULAR DELAY.** First out will be PageNet's VoiceNow service, developed with Motorola. This fall the company will test a new pager in New York, San Francisco, and Dallas that can receive voice messages, with a national rollout set for the first half of 1996. The price is a modest \$20 a month for local service, including the lease of the pager.

Callers trying to reach you simply dial an 800 number and leave a voice message, which is then transmit-

ted to the unit. The pager can store and play back up to four minutes of messages. But you can opt to have the network store additional messages for an as-yet-undetermined fee. When you clear out your old messages, the network will forward the new ones to you automatically.

BellSouth Mobilecomm is taking the concept a bit further. This fall it will launch ReadyTalk, developed by ReadyCom in Chapel Hill, N.C. While the ReadyTalk unit is clunkier than the VoiceNow pager, it lets you receive a voice message and send one back

### COMMUNICATIONS

Jersey regions in November.

Keep in mind that ReadyTalk makes use of open space on existing cellular frequencies. Hence, there could be problems transmitting voice messages inside buildings. Plus, when the frequencies are crowded with phone users, ReadyTalk messages take a backseat. So while most paging messages take a minute or so to transmit, a ReadyTalk message might take five minutes or more.

The unit stores up to 15 minutes of messages.

Of course, not everyone needs voice messaging; sometimes a simple text note will do just fine. But now you'll be able to respond with a text message of your own. Virtually all the big paging companies—including PageNet, BellSouth, SkyTel, PageMart, and AT&T—will be offering some form of two-way

## The Next Frontier in Paging

**PAGENET**  
800 PAGENET

Introduces VoiceNow voice pager in Dallas, New York, San Francisco this year; goes national in 1996; \$20/month with pager

**SKYTEL**  
800 SKYTEL7

Rolls out Skytel two-way pager on Sept. 19, letting users send and receive text; no price yet

**BELLSOUTH MOBILECOMM**  
800 769-1120

Offering ReadyTalk two-way voice pager in Southeast cellular markets this fall; \$30/month, excluding pager

**PAGEMART**  
800 324-PAGE

Begins two-way data paging by next summer; voice paging in the fourth quarter of 1996

DATA BUSINESS WEEK

to the person trying to reach you. Just talk into the pager to record a message, which is then forwarded to the number of the person who called.

BellSouth expects its service to cost less than \$30 a month, not including the pager, which will run \$250, or another \$7 a month. Initially, it will offer the service in the Southeast, where it provides cellular access. But ReadyCom is also licensing the technology to other cellular providers such as Comcast, which is expected to make ReadyTalk available in the Philadelphia and New

text paging early next year.

If the person paging you has a pager, he or she will get a beep confirming you received the message. In addition, you can send back one of several brief, preprogrammed messages to the person's pager or E-mail address. If the caller has neither, the message could be transmitted to a central voice mailbox and then forwarded to a home or office phone number, where a computerized voice could read the message out loud. Such services leave you fewer and fewer excuses to be out of touch.  
Mark Lewyn



## LOOK MA, NO PLANE TICKET

When passengers board United Airlines' domestic planes on Sept. 18, many of them will not be ticket holders. But they won't be gate-crashers, either. They'll be using an optional electronic ticketing system that UAL began offering on its California shuttles last November and is now extending to all its U.S. flights.

So-called E-tickets, stored in computer memory instead of printed on paper, are the latest innovation in air travel. Airlines expect to save millions of dollars by reducing the costs involved in issuing and processing paper tickets.

Continental Airlines, which began offering ticketless travel in April, 1995, has it on 50% of its domestic flights and will expand the service nationwide by yearend. American Airlines and



or change their routes just by using their phone and credit card. There is no paper document to worry about picking up, receiving in the mail, forgetting at home, losing, or having stolen. "Most of the time, our business travelers make last-minute changes to their routes or times of departure," says Mark Koehler, UAL's E-ticket project manager. With E-tickets, you can change your flight up to one hour prior to departure with just one call—though you still have to pay any extra charge for canceling your original ticket.

To reserve E-tickets, customers book their flights by phoning the airline's reservation center or a travel agent and paying with a credit card. If requested, they will receive an itinerary of the journey and a receipt by mail or fax. On the day of departure, passengers identify themselves at the airport ticket counter with a photo I.D., such as a driver's license or passport, or the credit card used to purchase the ticket. Some carriers, such as Southwest and Continental, give passengers a confirmation number as an extra security feature.

**CURBSIDE CHECK-IN.** Don't expect just to roll out of your car and onto the plane: Most E-ticket passengers still have to line up at ticket counters to check luggage and get a boarding pass. However, airlines are trying to speed up those procedures by allowing curbside check-in for ticketless travelers with photo IDs. Early next year, Continental and United also plan to install automated check-in machines that dispense boarding passes and assign seats; Continental's will even check luggage. Southwest ticketless passengers can go straight to the boarding gate if they have only carry-on bags.

One drawback is that only about 50% of travel agencies have a computer reservation system compatible with electronic ticketing. So there's a

good chance your agent can handle a ticketless booking. In fact, most ticketless travelers call airlines directly. "It works well for passengers traveling on routes with frequent flights and little variation in airfares," says Tanner, chief executive of Minneapolis-based Wagonlit, the second-

est U.S. agency. "But people like to shop around for the best price and schedule and need an agent to find the best deal."

If you are used to making your own arrangements, using online can help. United Connection and puServe allows you to view flight schedules, shop for fares, and purchase ticketless travel through your agent. An updated version will be available on the Microsoft Network next year and will be for sale on diskette in November. But E-tickets cannot currently be used on other consumer services, such as American Airlines' Easysabre, Worldspan Travel Service, operated by Delta, Travel Northwest.

So far, passengers have responded well. Southwest, for example, says 30% of its customers opt to go ticketless. Who says only millionaires with private planes can travel without a ticket in their pocket? *Silvia S.*

## Carriers That Go Ticketless

| AIRLINE                                | PROGRAM                                                                                                                             |
|----------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------|
| <b>ALASKA AIRLINES</b><br>800 426-0333 | Rolling out ticketless option to all 42 destinations in the Northwest and West by November                                          |
| <b>CONTINENTAL</b><br>800 525-0280     | E-ticketing available in 49 cities; will be expanded to most routes by yearend                                                      |
| <b>SOUTHWEST</b><br>800 435-9792       | Ticketless option offered on all flights throughout its 22-state route system                                                       |
| <b>UNITED</b><br>800 241-6522          | Beginning Sept. 18, will offer E-tickets on 2,000 daily domestic flights; ticketless passengers earn 500 bonus frequent-flier miles |
| <b>VALUJET</b><br>800 825-8538         | Pioneered ticketless travel two years ago; available on its 25 routes                                                               |

DATA BUSINESS WEEK

UAL, which is looking into expanding the service to international flights next year, is the first major carrier to make widespread use of ticketless travel. Atlanta-based ValuJet, a small regional airline, pioneered systemwide E-tickets two years ago, and regional Southwest Airlines started offering them on all its flights last January. Continental

Northwest will introduce E-tickets in a number of test markets in 1996.

UAL, which is enticing customers to try out the system with bonus frequent-flier miles, says electronic ticketing is aimed mainly at frequent fliers on short business trips. The advantage is that travelers can make reservations, buy tickets, get refunds,

## WORTH NOTING

**MAIL-ORDER PCs.** Are you looking to buy a personal computer by mail? The Better Business Bureau surveyed 27 nationally advertised direct-mail companies to compare price (on 90 Mhz Pentium systems), tech support hours and average wait times, and warranty and return policies. For a free copy, write the BBB of Metropolitan New York, 257 Park Avenue South, New York, N.Y. 10010.

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HAN YOU  
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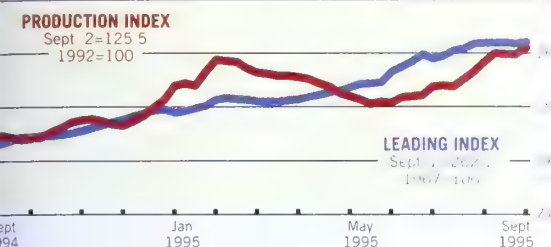
Financial Services, Information and Media, Educational and Professional Publishing



## PRODUCTION AND LEADING INDEXES

Change from last week: 0.5%  
Change from last year: 7.0%

Change from last week: 0.1%  
Change from last year: 7.9%



The production index rose in the week ending Sept. 2. Before calculation of the 4-week average, the index increased to 127.4, from 126.1 the week before. In the month of August, the index advanced to 125.4 from 123.3 in July. The leading index also rose in the latest week, pushed up by higher stock and lower bond yields. The unaveraged index increased to 262.6, from 261.8 the week before. For August, the index rose to 261.9, from 261.8 in July.

Production index copyright 1995 by The McGraw-Hill Companies. BW leading index copyright 1995 by CIBCIR.

## FINANCIAL INDICATORS

|                                    | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|------------------------------------|-------------|------------|--------------|
| PRICES (9/9) S&P 500               | 570.58      | 561.14     | 21.0         |
| FIXED RATE BOND YIELD, Aaa (9/9)   | 7.33%       | 7.39%      | -10.8        |
| RAW MATERIALS PRICES (9/9)         | 113.5       | 114.3      | NA           |
| INSURANCE FAILURES (9/1)           | NA          | NA         | NA           |
| FIXED RATE LOANS (8/30) billions   | \$495.4     | \$494.7r   | 11.9         |
| MONEY SUPPLY, M2 (8/28) billions   | \$3,709.8   | \$3,708.9r | 3.7          |
| CLAIMS, UNEMPLOYMENT (8/26) thous. | 349         | 348r       | 4.8          |

Sources: Center for International Business Cycle Research (CIBCIR), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures companies), Federal Reserve, Labor Dept. CIBCIR seasonally adjusts data on failures and real estate loans. \*Historical data available from CIBCIR.

## INTEREST RATES

|                                    | LATEST WEEK | WEEK AGO | YEAR AGO |
|------------------------------------|-------------|----------|----------|
| MONEY FUNDS (9/12)                 | 5.65%       | 5.86%    | 4.70%    |
| COMMERCIAL PAPER (9/13) 3-month    | 5.72        | 5.77     | 4.95     |
| SAVING DEPOSITS (9/13) 3-month     | 5.71        | 5.75     | 4.96     |
| MORTGAGE (9/8) 30-year             | 7.84        | 7.95     | 8.66     |
| FIXED RATE MORTGAGE (9/8) one-year | 5.85        | 5.86     | 5.56     |
| LIBOR (9/13)                       | 8.75        | 8.75     | 7.75     |

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### INVENTORY TRENDS

**Sept. 18, 10 a.m. ▶** Inventories of manufacturers, wholesalers, and retailers are expected to show a 0.4% increase in July, according to the median forecast of economists surveyed by MMS. In June, one of the McGraw-Hill Cos. surveys had risen 0.2% in June. If the increase is on the mark, inventories would be the third quarter rising slightly less than the average second-quarter pace, suggesting that businesses continue to rein in inventory growth.

### NEW HOME STARTS

**Sept. 19, 8:30 a.m. ▶** Builders' confidence in new homes at an annual

rate of 1.38 million units in August, the same as in July, say the forecasters. July starts had surged to the highest level of the year, as lower interest rates boosted sales.

### INTERNATIONAL TRADE

**Wednesday, Sept. 20, 8:30 a.m. ▶** The trade deficit for goods and services is expected to have narrowed a bit in July, to \$10.9 billion, from \$11.3 billion in June, say the economists. If so, the trade gap would begin the third quarter a shade below the second-quarter average, so trade may not be as big a drag on economic growth as it was in the second quarter. July exports are expected to have advanced, while imports apparently held steady.

## PRODUCTION INDICATORS

|                                                | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|------------------------------------------------|-------------|-----------|--------------|
| STEEL (9/9) thous. of net tons                 | 1,984       | 1,949#    | 10.4         |
| AUTOS (9/9) units                              | 112,401     | 118,296r# | 0.5          |
| TRUCKS (9/9) units                             | 99,189      | 105,651r# | -4.7         |
| ELECTRIC POWER (9/9) millions of kilowatt-hrs. | 66,148      | 72,418#   | 10.5         |
| CRUDE-OIL REFINING (9/9) thous. of bbl./day    | 14,730      | 14,282#   | 2.3          |
| COAL (9/2) thous. of net tons                  | 20,705#     | 20,317    | -1.2         |
| PAPERBOARD (9/2) thous. of tons                | 837.7#      | 889.9r    | -6.5         |
| PAPER (9/2) thous. of tons                     | 847.0#      | 850.0r    | -0.9         |
| LUMBER (9/2) millions of ft.                   | 457.2#      | 465.9     | -3.6         |
| RAIL FREIGHT (9/2) billions of ton-miles       | 25.7#       | 25.0      | 4.5          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA<sup>1</sup>, SFPA<sup>2</sup>, Association of American Railroads

## PRICES

|                                                    | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|----------------------------------------------------|-------------|----------|--------------|
| GOLD (9/13) \$/troy oz.                            | 384.900     | 380.050  | -1.5         |
| STEEL SCRAP (9/12) #1 heavy, \$/ton                | 143.50      | 146.50   | 6.7          |
| COPPER (9/8) ¢/lb.                                 | 136.2       | 137.3    | 12.3         |
| ALUMINUM (9/8) ¢/lb.                               | 82.5        | 85.5     | 8.8          |
| COTTON (9/8) strict low middling 1-1/16 in., ¢/lb. | 88.56       | 90.55    | 22.1         |
| OIL (9/12) \$/bbl.                                 | 18.73       | 18.51    | 12.2         |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                                  | LATEST WEEK | WEEK AGO | YEAR AGO |
|----------------------------------|-------------|----------|----------|
| JAPANESE YEN (9/13)              | 102.59      | 98.74    | 99.23    |
| GERMAN MARK (9/13)               | 1.50        | 1.48     | 1.55     |
| BRITISH POUND (9/13)             | 1.55        | 1.55     | 1.56     |
| FRENCH FRANC (9/13)              | 5.15        | 5.09     | 5.30     |
| ITALIAN LIRA (9/13)              | 1617.0      | 1621.5   | 1563.8   |
| CANADIAN DOLLAR (9/13)           | 1.35        | 1.34     | 1.35     |
| MEXICAN PESO (9/13) <sup>1</sup> | 6.285       | 6.240    | 3.406    |

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

## FEDERAL BUDGET

**Friday, Sept. 22 ▶** The federal budget for August is expected to have been in deficit by \$28 billion, up from August, 1994's red ink of \$24.3 billion. The deficit for the first 10 months of the fiscal year totaled \$133.9 billion. The August projection would bring the deficit's 12-month moving sum to \$161.1 billion, suggesting that the budget gap is on target to hit the Congressional Budget Office's latest projection of \$161 billion. That would bring the deficit down to 2.3% of gross domestic product, the lowest in relation to the size of the economy since 1979. Improvement in the most recent years stems mainly from increased receipts, reflecting the strength of the economy.



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## This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

**Sunday** Win95 and multimedia got you thinking of a new PC for your home? Find out the latest on the PC marketplace from Andy Bose of Link Resources and Gary McWilliams of Business Week. **Sept. 17 9 p.m. EDT in the Globe**

**Wednesday** Interview author Kurt Eichenwald of the best-seller *Serpent on the Rock*, about how Prud-Bache limited partnerships put the bite on investors. **Sept. 20 8 p.m. EDT in the Globe**

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event. For a free trial diskette including 10 free hours on AOL, call 1-800-641-4848 and mention Business Week.



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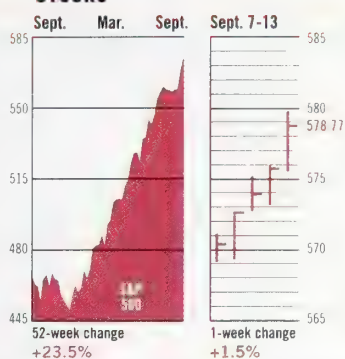
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# Investment Figures of the Week

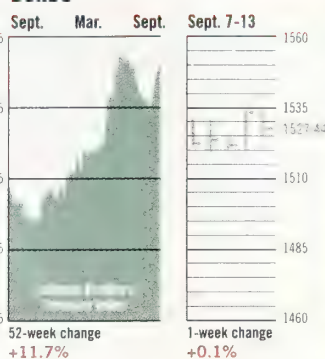
## TARY

no stopping this mar-  
major indexes hit highs,  
ut twice during the week.  
rd & Poor's 500-stock  
a nifty 1.5%, while the  
rials jumped 1.7%. What  
ssive about the Dow's  
e is that IBM, a major  
nent, was down 6 points  
k, the result of the com-  
ncing that third-quarter  
estimates were too high.  
stock rally: the recent  
interest rates, continuing  
duced inflation, and the  
dollar.

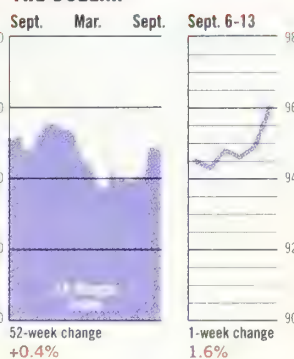
## STOCKS



## BONDS



## THE DOLLAR



## ET ANALYSIS

| STOCKS                       | Latest | Week | % change<br>52-week |
|------------------------------|--------|------|---------------------|
| INDUSTRIALS                  | 4765.5 | 1.7  | 22.3                |
| COMPANIES (S&P MidCap Index) | 217.5  | 1.0  | 23.6                |
| COMPANIES (Russell 2000)     | 316.0  | 1.7  | 22.7                |
| COMPANIES (Russell 3000)     | 334.2  | 1.5  | 23.9                |

| STOCKS              | Latest   | Week | % change (local currency)<br>52-week |
|---------------------|----------|------|--------------------------------------|
| FINANCIAL TIMES 100 | 3570.8   | 0.4  | 15.9                                 |
| NIKKEI INDEX        | 18,614.3 | 5.6  | -6.6                                 |
| EURO COMPOSITE      | 4586.9   | 0.3  | 5.6                                  |

## FUNDAMENTALS

|                              | Latest | Week ago | Year ago |
|------------------------------|--------|----------|----------|
| 90-DAY TREASURY BILL YIELD   | 5.45%  | 5.48%    | 4.68%    |
| 30-YEAR TREASURY BOND YIELD  | 6.52%  | 6.59%    | 7.67%    |
| S&P 500 DIVIDEND YIELD       | 2.34%  | 2.37%    | 2.71%    |
| S&P 500 PRICE/EARNINGS RATIO | 16.7   | 16.4     | 18.6     |

|                                           | Latest | Week ago | Reading  |
|-------------------------------------------|--------|----------|----------|
| S&P 500 200-day moving average            | 511.8  | 508.8    | Positive |
| Stocks above 200-day moving average       | 79.0%  | 77.0%    | Negative |
| Speculative sentiment: Put/call ratio     | 0.52   | 0.54     | Negative |
| Insider sentiment: Vickers sell/buy ratio | 2.30   | 2.35     | Neutral  |

BLOOMBERG FINANCIAL MARKETS

## TRY GROUPS

| LEADERS                | 1-month | 12-month | Strongest stock in group | 1-month | 12-month | Price                          |
|------------------------|---------|----------|--------------------------|---------|----------|--------------------------------|
| AL LOANS               | 14.2    | 44.5     | HOUSEHOLD INTERNATIONAL  | 15.2    | 56.9     | 59 <sup>5</sup> / <sub>8</sub> |
| ICATIONS EQUIPMENT     | 12.3    | 75.0     | CISCO SYSTEMS            | 22.0    | 186.2    | 71 <sup>5</sup> / <sub>8</sub> |
| S AND LOANS            | 11.5    | 15.4     | GREAT WESTERN FINANCIAL  | 14.5    | 19.5     | 23 <sup>3</sup> / <sub>4</sub> |
| MENT BANKING/BROKERAGE | 11.3    | 39.6     | DEAN WITTER, DISCOVER    | 19.4    | 36.9     | 57                             |
| INE INSURERS           | 11.1    | 38.0     | AETNA LIFE & CASUALTY    | 12.0    | 45.7     | 70 <sup>1</sup> / <sub>8</sub> |

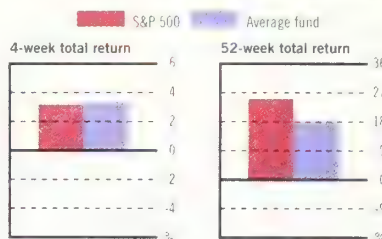
| LAGGARDS     | 1-month | 12-month | Weakest stock in group | 1-month | 12-month | Price                          |
|--------------|---------|----------|------------------------|---------|----------|--------------------------------|
| WARES        | -2.3    | 11.8     | RUBBERMAID             | -3.7    | 9.9      | 29 <sup>1</sup> / <sub>4</sub> |
|              | -1.9    | 13.0     | BROWN GROUP            | -22.5   | -48.7    | 19                             |
| TER SYSTEMS  | -1.8    | 47.0     | IBM                    | -10.8   | 43.7     | 97 <sup>1</sup> / <sub>8</sub> |
| TY RETAILERS | -1.4    | -5.0     | HOME DEPOT             | -5.6    | -8.0     | 40 <sup>1</sup> / <sub>8</sub> |
|              | -1.2    | 23.3     | MATTEL                 | -2.1    | 36.1     | 29 <sup>1</sup> / <sub>4</sub> |

## AL FUNDS

| total return            | %    | LAGGARDS                      | Four-week total return | % |
|-------------------------|------|-------------------------------|------------------------|---|
| Y SELECT COMPUTERS      | 12.0 | WRIGHT EQUIFUND-SPAIN         | -4.8                   |   |
| X ASIA INFRASTRUCTURE A | 11.9 | EV MARATHON GREATER INDIA     | -4.7                   |   |
| ESSIVE ENVIRONMENTAL    | 11.8 | DFA CONTINENTAL SMALL COMPANY | -3.6                   |   |

| total return         | %     | 52-week total return                | %     |
|----------------------|-------|-------------------------------------|-------|
| Y SELECT ELECTRONICS | 106.3 | WRIGHT EQUIFUND-MEXICO              | -45.9 |
| SMALLER COMPANIES A  | 97.3  | BT INVESTMENT LATIN AMERICAN EQUITY | -36.6 |
| CAPITAL APPRECIATION | 96.4  | HERCULES LATIN AMERICAN VALUE       | -35.0 |



## FIVE PORTFOLIOS

ounts represent the  
ue of \$10,000  
ne year ago  
portfolio

ges indicate  
otal returns

**U.S. stocks**  
**\$12,633**  
+1.29%

**Treasury bonds**  
**\$12,433**  
+0.43%

**Foreign stocks**  
**\$11,007**  
+0.48%

**Money market fund**  
**\$10,538**  
+0.12%

**Gold**  
**\$9,902**  
+0.98%

his page is as of market close Wednesday, Sept. 13, 1995, unless otherwise indicat-  
groups include S&P 500 companies only; performance and share prices are as of mar-

ket close Sept. 12. Mutual fund returns are as of Sept. 8. Relative portfolios are valued as of Sept.  
12. A more detailed explanation of this page is available on request. r=revised NA=Not available



## THE OTHER SHAME OF BOB PACKWOOD

**T**he diaries of Senator Bob Packwood show that his political life was as sleazy as his private one. The documents are a sad chronicle of abuse of power and a misbegotten mix of campaign contributions and special tax legislation. If this scandalous kind of influence-peddling is typical of Washington behavior (as *Friends in High Places*, the latest book on insider Clark M. Clifford, tells us it is), then lobbying and campaign-finance reforms must come at once.

The Packwood diaries are a window into a legislative chamber of horrors. His drinking buddies were lobbyists who used their access to the senior Republican on the tax-writing Senate Finance Committee. The lobbyists raised cash for Packwood campaigns while their clients had issues pending before the committee. In the diaries, Packwood admits to a lobbyist for Shell Oil Co. that he was doing him a favor by getting a special oil tax bill passed. The man was a close personal friend who raised money for his reelection.

Before the Senate Ethics Committee investigating his behavior, Packwood insisted: "I don't trade my vote for money." But according to the diaries, that didn't stop him from asking a lobbyist for one foreign company for a \$7,500-a-year retainer for Packwood's soon-to-be-divorced wife.

Packwood does not stand alone in his cynical attitude. For too long, senators and congressmen have confused clients' interests with national interests and personal favors with principle. Even now, the House, under Newt Gingrich (R-Ga.), refuses to take up lobbying reform, and the greediest gorgers on PAC money these days are the freshmen Republicans elected in 1994 on a platform of changing Washington. How sad it is to see them in Congress, shoulder-to-shoulder with lobbyists, thanking them for helping write legislation that will only benefit their clients.

What's needed now is an aggressive, three-pronged effort to cleanse the cauldron. First, special-interest money should be

eliminated as quickly as possible. The House should follow lead of the Senate, which already has passed legislation ending an era of Caribbean cruises paid for by special-interest groups. The Senate also has passed legislation that forces lobbyists to disclose their activities, and for the first time requires those who lobby the executive branch to list themselves as lobbyists. This would reinforce President Clinton's recent executive order on White House lobbyist disclosure requirements.

Second, the penalties for evading existing donation rules should be toughened, including much larger fines and longer prison terms. The Packwood diaries outlined how so-called "independent" expenditures are often illegally coordinated with a campaign—so a group can spend far more than the limit on behalf of a candidate. Also, "soft money" (which by law is to be used for building party organizations) is funneled improperly to specific campaigns, as Democratic then-National Republican Senatorial Committee member Phil Gramm of doing for Packwood in the 1992 election. These soft-money contributions allow corporations, unions, and large individual contributors to evade donation limits by giving hundreds of thousands of dollars to party organizations. This is wrong and should be stopped immediately.

Campaign reform is trickier. Fully financing campaigns with tax dollars would be expensive—costing perhaps \$1 billion—and unlikely ever to pass Congress. A reasonable alternative would be to limit the maximum contribution to political action committees to the same level as individual contributions—\$1,000 now. That would reduce—but not eliminate—the money flow. In addition, there should be a voluntary spending limit. If one candidate spends over the limit, tax money would be provided to his or her opponent. The Packwood diaries show just how deep the corruption runs. It's time to do something about it.

## REAPPOINT ALAN GREENSPAN

**O**ver the next six months, two extraordinary things will happen. Legislation to balance the federal budget will pass, and three slots will be open at the Federal Reserve, including Alan Greenspan's spot as Fed chairman. Who will guide the nation's monetary policy over the next few years will be even more important than usual. That is why Clinton should reappoint Greenspan, who has done a good job in a difficult period. At the same time, he should fill the other two slots with governors who understand how the economy is changing.

A budget that moves toward balance over a period of years will dramatically shift the mix of fiscal and monetary policies needed to assure the continued prosperity of the nation. A shrinking deficit means a drag on the economy, at least

in the short run, as government jobs are eliminated and funds for Medicare and other programs are cut. So this will presumably be cushioned by a drop in long-term interest rates, which will stimulate investment. But the Fed must stand ready to be an active player as well, if it is necessary to cut short-term rates to compensate for the stimulus from government spending.

Such talk is anathema to Senate Republicans. With the Fed already open, and Vice-Chairman Alan S. Blinder apparently ready to return to Princeton University, there are signs the Republicans will reject any nominee who is not tough enough on inflation. An economic litmus test for the Federal Reserve Board may be good politics, but it won't serve the best interests of U.S. workers and businesses.



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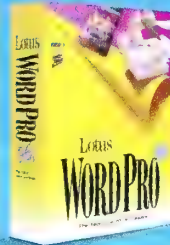
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Step 1 Who \ Step 2 What \ Step 3 How \

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☒ Set options for all people to Review and Comment ☒ Display Greeting with this text  
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SS WEEK  
October 2

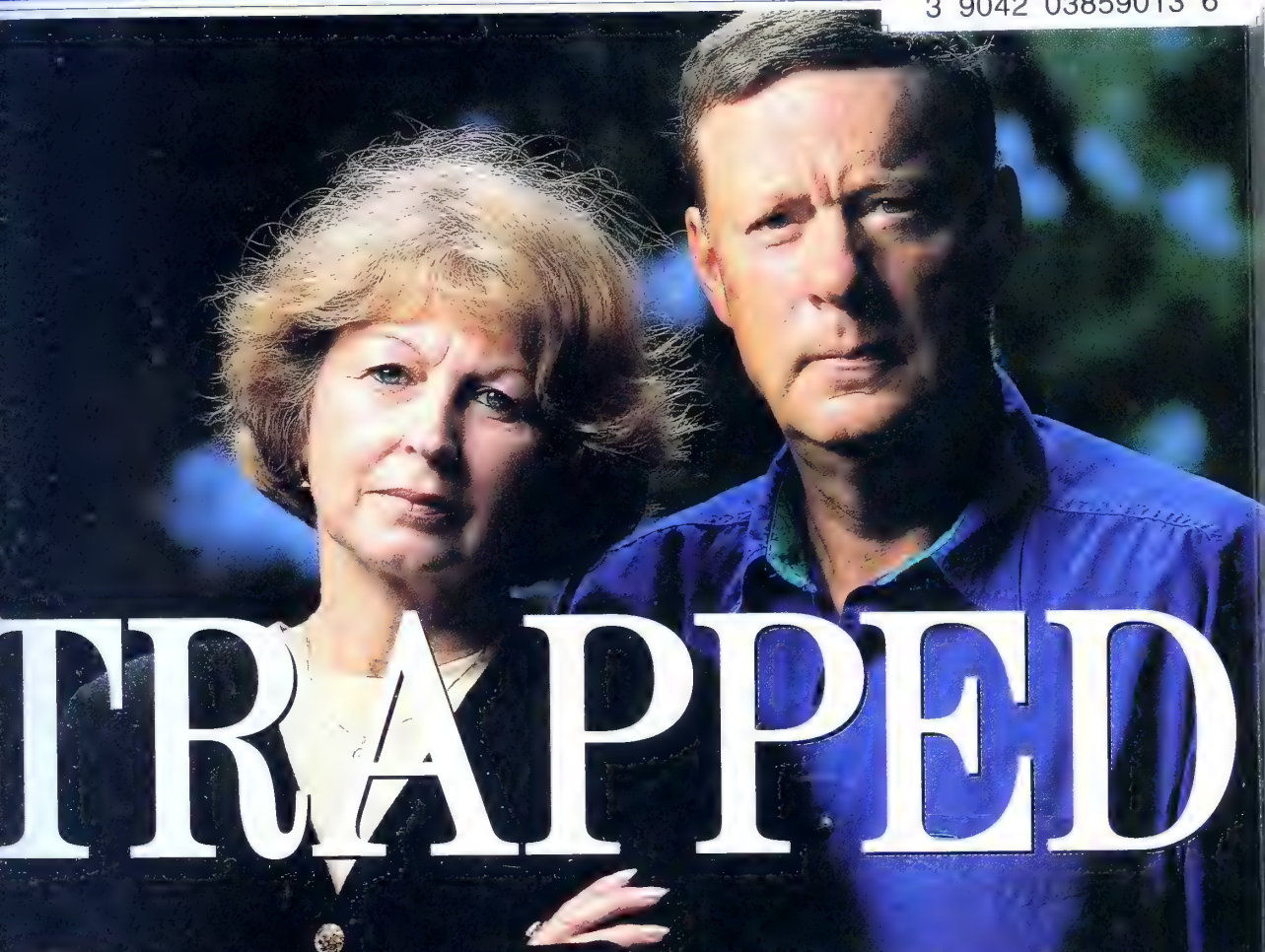
# BusinessWeek

ER 2, 1995

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# TRAPPED

John Swanson shaped Dow Corning's vaunted ethics program. His wife, Colleen, was certain that Dow Corning breast implants were destroying her health—and that the company had failed to inform women of the risks.

is their wrenching story.

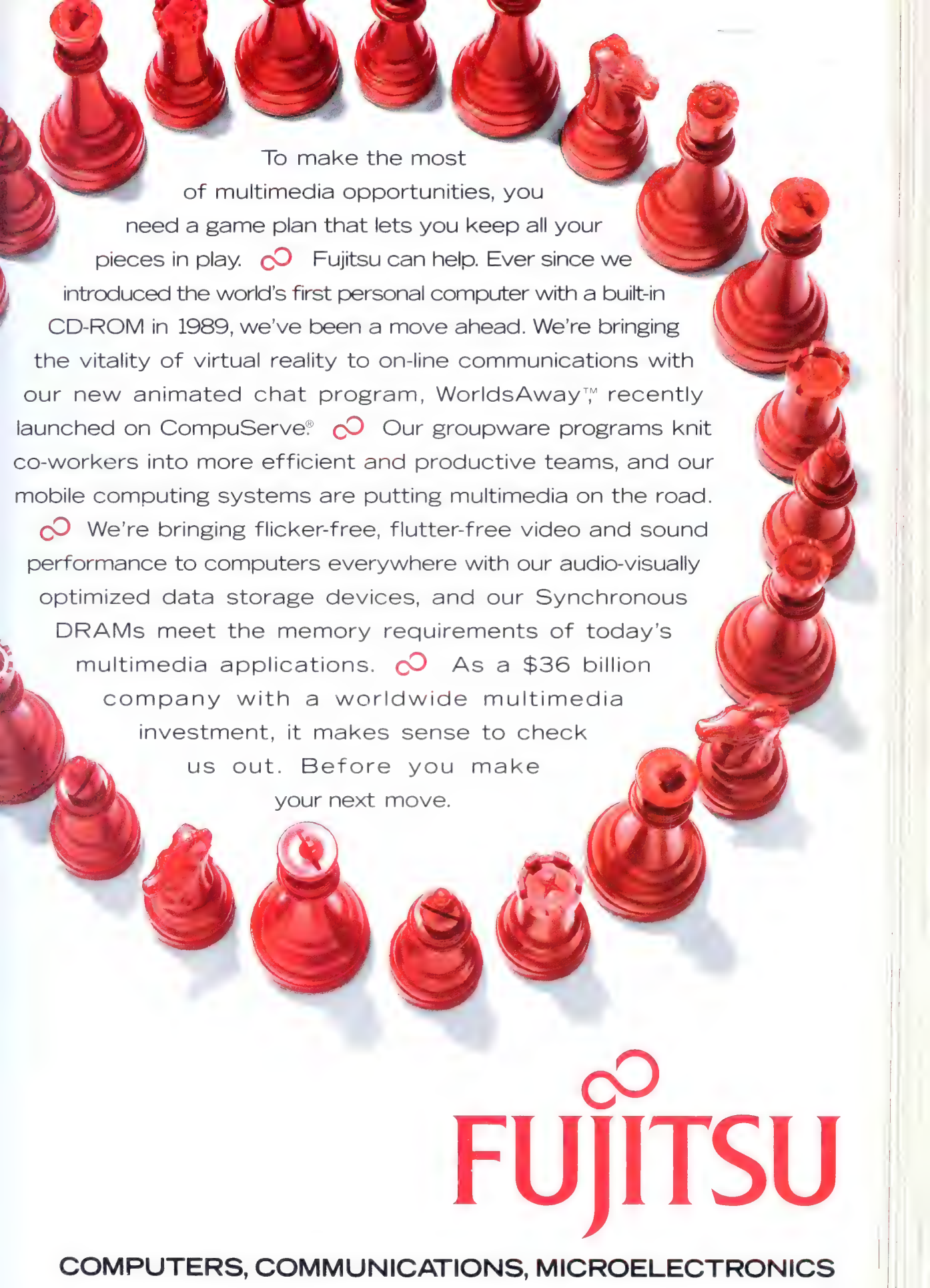
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company with a worldwide multimedia  
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$\frac{20}{200}$

**IF**

$\frac{200 \text{ FT}}{61 \text{ M}}$

**1**

$\frac{20}{100}$

**U READ**

$\frac{100 \text{ FT}}{30 \text{ M}}$

**2**

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**THIS U CAN**

$\frac{70 \text{ FT}}{21 \text{ M}}$

**3**

$\frac{20}{50}$

**GET MORE**

$\frac{50 \text{ FT}}{15 \text{ M}}$

**4**

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**V A L U E 4**

$\frac{40 \text{ FT}}{12 \text{ M}}$

**5**

$\frac{20}{30}$

**Y O U R M O N E Y**

$\frac{30 \text{ FT}}{9 \text{ M}}$

**6**

**K E M O R E**

**7**

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COVER ST

**TRAPPED**  
What happens when a Dow Corning engineer, steeped in the company's culture, starts to believe his wife's breast implants made her sick?

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OCTOBER 2, 1995

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As John Swanson shaped the ethics program at Dow Corning, his wife, Colleen, fell ill after receiving Dow Corning breast implants. Here, in an adaptation from a forthcoming book by Senior Writer John Byrne, is an account of the Swansons' harrowing dilemma

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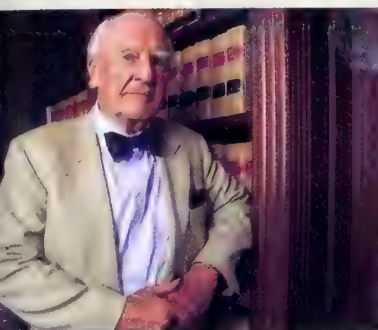
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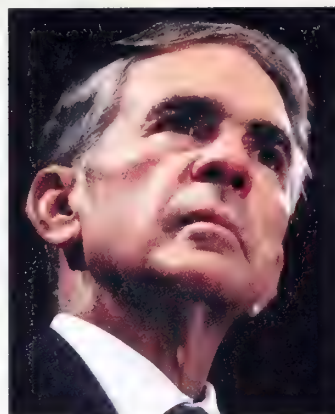
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## DE WALL STREET

...d Ivax get swallowed?  
...me ye to Bethlehem  
Source tunes in

## STMENT FIGURES OF THE WEEK

## ple

## IN DISNEY'S UNKNOWN STARS

...ack and Bollenbach, both relative  
comers to Disney, are the ones who  
make the ABC deal go

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## CARE'S POST-OP CARE

...NESS WEEK offers prescriptions for  
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make the system fairer

## ormation Processing

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Home shopping without TV

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The last word on grits, by Uncle Sam



# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

## KIBITZERS

### ADM'S BIG INVESTORS GROW RESTLESS

IN THE FACE OF THREE grand jury probes, Archer Daniels Midland's strategy has been to say little. But now, two influential stockholders—the public-worker pension funds for California (holding 3.4 million ADM shares) and New York City (2.7 million)—are demanding to know what the board's doing. Their likely next step if they're not

satisfied: to target individual directors for face-to-face meetings. Other institutional investors may follow.

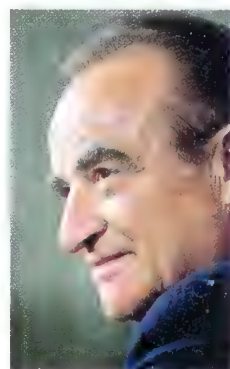
At issue are allegations of price-fixing in food additives by a onetime senior executive-turned-FBI informant. A key question: how independent are the outside directors, most of them longtime friends of powerful ADM Chairman Dwayne

**TALK SHOW** "Other than [being] served with a lawsuit during my clam chowder, it was a very productive meeting!"

—Dallas Cowboys owner Jerry Jones, after meeting with the NFL, which is suing to stop his solo sponsorship deals

Andreas. ADM's outside directors, led by ex-Canadian Prime Minister Brian Mulroney, are conducting their own inquiry—and, says his spokesman, "working diligently."

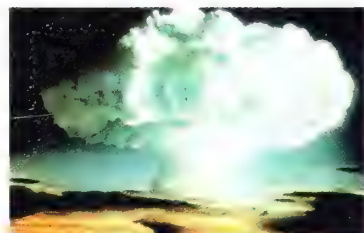
While the funds each hold less than 1% of ADM, they're among its largest investors. New York City Comptroller Alan Hevesi has written Andreas complaining that the board "has been vir-



**ANDREAS:** No loyal opposition

tually silent." Separately, the California Public Employees' Retirement System's investment board has approved sending a similar message. Meanwhile, the Council of Institutional Investors

an umbrella group representing 100 large pension funds is considering pressuring ADM. *Richard Melton*



**SNAG:** No tritium, no boom

## TAXES AT WORK

### CAUTION: RADIOACTIVE PORK

WASHINGTON IS WORRIED IT'S running out of tritium, the essential ingredient in thermonuclear warheads. So Energy Secretary Hazel O'Leary is expected to announce a deal soon that will keep the U.S. arsenal potent—and also please two key GOP senators by giving both their home states the action.

Senate Armed Services Committee Chairman Strom Thurmond (R-S.C.) wants any new tritium-production facility to be located in South Carolina. "We've got the expertise," says an aide. Senate Budget Committee Chairman Pete Domenici (R-N.M.) wants any research on tritium-making methods to be done at New Mexico's Los Alamos National Laboratory, which has nuke experience. Initial price tag for this multibillion-dollar program:

\$50 million in fiscal 1996.

The feds closed their aging tritium plant in 1988 at Savannah River, S.C. Even though pending treaties would reduce the nuclear arsenal, experts say the U.S. must start exhausting its limited-supply tritium stockpile by 2005. Tritium is good for up to 12½ years, and then it has to be replaced. *Mary Beth Regan*

## CONTINENTAL DRIFT

### FRANCE TELECOM KEEPS LOSING ITS HEAD

AT FRANCE'S STATE-OWNED enterprises, boardroom coups are nothing new. Recent upheavals at France Télécom, though, are exacting a heavy price. Until the chaos ends, France will slip behind as other nations prepare phone utilities for 1998's

Europewide deregulation.

This summer, Post & Telecommunications Minister François Fillon managed to depose Télécom President Marcel Roulet, who pushed for rapid privatization. Successor François Henrot, president of Compagnie Bancaire, resigned in protest after a promised union leaders' delay in selling a minority stake to investors. To repair the damage, Prime Minister Alain Juppé quickly named yet another new president: the pro-privatization Michel Bon, former chief of retail Carrefour.

Unions fear that a sale would bring in stockholders eager to end job guarantees and automatic pay hikes. A hoped-for public offering first slated for next year will now be delayed until 1997, at the earliest. By then, alas, stock markets throughout Europe will be flooded with \$30 billion in offerings from Germany's Deutsche Telekom and others. *Gail Edmondson*

## THE LIST BULL RUN



**ON A ROLL:** Wall Street

The stock market is hot and—no surprise—so are brokerage shares. Their 1995 performance ranks No. 5 among the 20 Standard & Poor's index groups, with semiconductors on top. Discounters such as Charles Schwab do well in bull markets, thanks to big retail volume. Alex. Brown & Sons, a specialist in initial public offerings, is riding the wave of high-tech issues. Salomon Brothers, focused on trading and investment banking, is suffering from defections of stars.

### HOW BROKERAGES ARE RIDING THE MARKET

| TOP FIVE<br>(STOCK SYMBOLS) |                 |                  | BOTTOM FIVE<br>(STOCK SYMBOLS) |                 |                  |
|-----------------------------|-----------------|------------------|--------------------------------|-----------------|------------------|
|                             | STOCK*<br>PRICE | 1995**<br>CHANGE |                                | STOCK*<br>PRICE | 1995**<br>CHANGE |
| CHARLES SCHWAB (SCH)        | 26½             | 130%             | A.G. EDWARDS (AGE)             | 24½             | 34%              |
| QUICK & REILLY (QOR)        | 40½             | 115              | PAINWEBBER (PWJ)               | 19½             | 28               |
| WATERHOUSE (WHO)            | 23½             | 107              | SCOTT/STRINGFELLOW (SCOT)      | 13              | 18               |
| ALEX. BROWN (AB)            | 58              | 91               | ZIEGLER (ZCO)                  | 16½             | 8                |
| MERRILL LYNCH (MER)         | 61½             | 73               | SALOMON (SB)                   | 38½             | 2                |

\*On Sept. 18, 1995

\*\*From Jan. 1 through Sept. 18, 1995, for 22 publicly traded brokerages with 1994 closing price over \$10 per share, adjusted for splits

DATA: SECURITIES DATA CO. BLOOMBERG FINANCIAL MARKETS

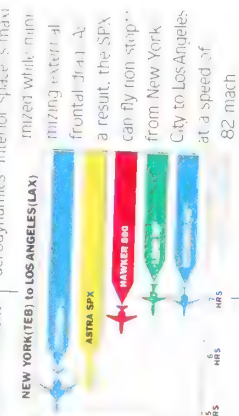


Citation X

# What price speed?

The new Astra SPX is not just fast in its class, it's fast in any class. BICA says, "The SPX's speed on trans-continental flights should be competitive with the fastest business jets -- regardless of size or price."

When the Astra SPX touches down at LAX on a non-stop flight from New York, it is only 19 minutes behind the Citation X. The next competitor is just entering Arizona airspace. The SPX time is one hour faster than the other manufacturer's aircraft. The Lear 60 and Citation



VI require a stop\*\* to complete the mission. Astra SPX is the business jet that makes the others up in the air. SPX brings a whole new dimension to the world of business aviation. Built of advanced technology, the fuselage fits the human form and achieves the highest degree of aerodynamics. Interior space is maximized while minimizing external frontal drag. As a result, the SPX can fly non-stop from New York City to Los Angeles at a speed of 82 mach.

## Climb to the top

Thanks to the new five-engine, high-altitude Astra SPX, the SPX is a jet that makes the others up in the air. SPX brings a whole new dimension to the world of business aviation. Built of advanced technology, the fuselage fits the human form and achieves the highest degree of aerodynamics. Interior space is maximized while minimizing external frontal drag. As a result, the SPX can fly non-stop from New York City to Los Angeles at a speed of 82 mach.

midsize competitors. In fact, the SPX can take off from shorter fields than the Beejet 400A and has a lower operating cost per mile than the Citation V Ultra.

## Sweet Suite

The Astra SPX has one of the most versatile and adaptable interiors ever. It has 11 configurations at the moment. Says BICA, "The Astra SPX's Pro Line 4 amenities, in our opinion, is one of the most intuitive layouts we've ever seen. This is Pro Line 4 at its best." Equipped with top 7.5-inch CRT displays, a color Primary Flight Display, and a color engine data display, it's a cockpit that gives you

pilots will quickly feel at home in the cockpit.

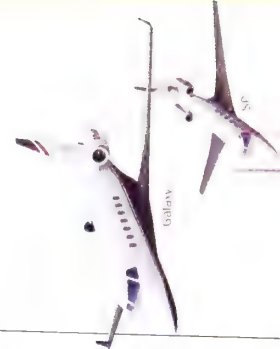
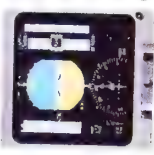
## Your CFO will approve

"The Astra SPX will score an A+ in the knots-per-dollar-of-purchase-price category on the chief financial officer's tally card."

says BICA. The Astra SPX is part of a new generation of Astra business aircraft designed for corporations, large and small, looking for new ways to reduce overhead and improve profits. After all, it always comes down to the bottom line.

## WHAT PRICE SPEED?

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## HONCHOS

### SANDY WEILL'S BURNING AMBITION

AS SUMMER FADES, SANFORD Weill looks forward to once more indulging his love of a crackling fire—at work. The Travelers chief executive recently had a fireplace built in his new offices in Lower Manhattan. Dominating the library between Weill's office and Travelers President James Dimon's, the hearth's glow gives a homey feel to

## TOASTY: Skyscraper hearth

a center of financial power.

This is Weill's fourth office fireplace, all of them in modern office towers. The first was built in the 1970s, when Weill ran Shearson, on the 106th floor of the World Trade Center—earning it a place in the *Guinness Book of World Records* as the world's highest working fireplace. As American Express' president in the mid-1980s, Weill had one installed in the World Financial Center. Next, as Primerica's CEO, he put one in the midtown IBM Building. Weill says he doesn't know how much a New York office fireplace costs, but installers say it can range from \$12,000 to \$16,000.

What's his fascination with fire? Weill likes to gather around the hearth with employees or clients and unwind. Says Weill: "It takes a tense environment and makes it more relaxed and thoughtful." *Leah Nathans Spiro*

## CAR TALK

### PLYMOUTH WILL OFFER VROOM WITH A VIEW

DETROIT'S WORST-KEPT SECRET is revving up. Before year-end, Chrysler insiders say, the auto maker will announce that the Plymouth Prowler will go on sale in the next model year or two. A retro-

Plymouth's sparse product line could use a boost. The division now sells only the Neon subcompact and Voyager minivan, with the Breeze compact to be added for the 1996 model year. Publicly, Chrysler is coy about the Prowler's future. But suppliers insist the Prowler is due out in 1997 or 1998 at the latest.

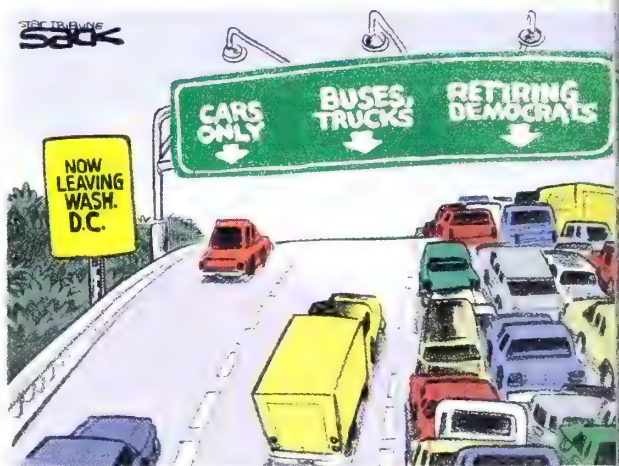
The rear-wheel-drive Prowler will be powered by a 3.5-liter, V-6 engine and boast lightweight aluminum body parts. Price tag: about \$35,000, high for the entry-level car buyers Plymouth targets. Still, Chrysler hopes the car will wow the public, as it has enthusiasts on the auto-show circuit, where it's shown as a novelty. *Bill Vlasic*



**PROWLER:**  
Coming attraction

styled roadster that evokes the hot rods of the 1950s, the much-awaited Prowler is supposed to jazz up Chrysler's Plymouth brand the way the Viper muscle car elevated the image of the Dodge Div.

## DRAWN & QUARTERED



## POP PSYCH 101

### PIGEONHOLING GOES CORPORATE

YOU'VE NEVER HEARD OF enneagrams? You may soon. This system of personality analysis, once faddish pop psychology, is becoming a personnel tool for

Corporate America. The enneagram (pronounced any-a-gram) system, whose origins are obscure, types people into nine personality groups, using a written test. It's similar to the oft-used Myers-Briggs test, but enneagram fans say their test is more in-depth.

Greek for "nine" and "drawing," the enneagram is a nine-pointed star with a

personality type at each point. Every type has pluses and minuses. A One, or Perfectionist, is conscientious but can't handle criticism. An Eight, the Asserter, is energetic—plus abrasive. Knowing your own and others' numbers is supposed to make both bosses and underlings cooperate better.

For \$1,000 a participant, Doyle-Farney in Hartford conducts five-day programs at Hewlett-Packard and other companies. Says Dominick Robertson, who had 10 people from the HP division head the course, a better "to talk about your type than about aspects of your personality that irritate me." *Julie Tilsner*



## THE BIG PICTURE

### ALL WORK AND NO PLAY

What vacation? Of employed Americans vacationing this summer, 23% (or 29 million) performed some work.

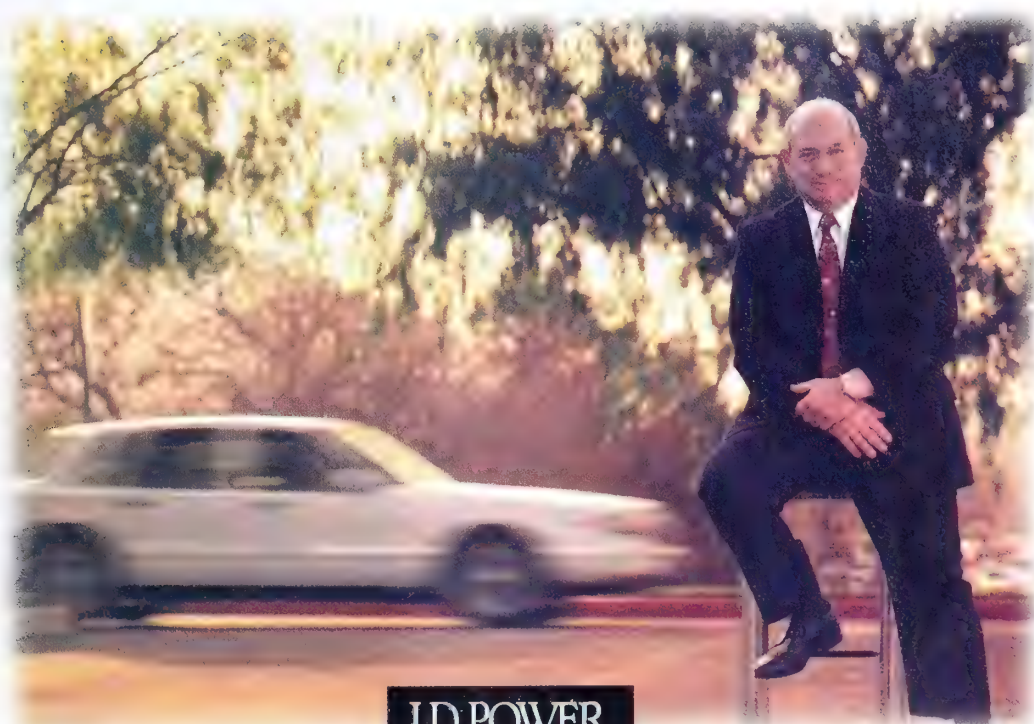
Here is what they did, according to a survey; some did more than one job-related task.



DATA: STEELCASE INC.



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**Will the cars on the drawing board today meet consumer demands of tomorrow? That's the question facing J.D. Power and Associates. The answers are coming from the SAS System.**

"We produce a monthly forecast of car and truck sales for about 300 different vehicles," says Jon Rosenthal, Manager of Automotive Forecasting for J.D. Power and Associates. "Each vehicle is forecasted by month for five years beyond the current year. Right now I'm forecasting through the year 2000."

## ***The SAS System Fits Our Business***

"The SAS System is the fuel behind those forecasts...our software of choice for analyzing sales, economic, and auto industry data and then reporting what we've learned," adds Rosenthal. "Before the SAS System, much of the forecasting was done by hand. To make our forecasts credible, we had to have a credible system. One that made it easy to build applications and put them to work across our computing environments. We've got minis, Macs, desktop publishing, and a lot of spreadsheets. The SAS System fits the way we do business."

## ***The Bottom Line is Information***

Now that the forecasting model is up and running, Rosenthal and his staff are using the SAS System to build an interactive database. "The Power Information Network will allow an auto dealer or manufacturer to go online and get market information," Rosenthal explains. "When released,

subscribers will be able to select from a long menu of reports and data. The versatility of the SAS System is crucial in developing the reports."

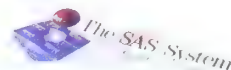
"The bottom line is this: applications are being developed with the SAS System that will deliver the most up-to-date information to those who make decisions for the automotive industry," says Rosenthal. "If manufacturers and dealers can get their hands on accurate market information and predictions, they have a much better chance of meeting customers' needs down the road."

**To receive a SAS System Executive Summary, give us a call or visit us on the World Wide Web at <http://www.sas.com>**



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## QUOTAS MAY DISAPPEAR. INEQUALITY WON'T

After carefully reading "Quotas: A bad idea whose time has gone" (Economic Viewpoint, Sept. 11), I could not agree more. But [Paul Craig Roberts'] reasons for wanting to eliminate quotas are different from mine. I believe it would be good for African Americans to have the quota system phased out, but only when the playing field is level.

If Roberts thinks it is already level, he should remove his rose-colored glasses. The past 200 years have seen a system in which highly qualified African Americans were not offered jobs—in many cases not even considered—and the jobs were given to less qualified white males.

We do have a caste society, but it doesn't favor African Americans.

Bernard M. Curtis  
Walnut, Calif.

The U.S. Constitution is color-blind, but people aren't—not in America, not in Japan, not in the world. Quotas are theoretically a bad idea, but in the concrete world of prejudice they are necessary. Nineteen years ago, I was hired because the company needed one white male. How's that for irony?

Michael G. Driver  
Ichihara City, Japan

## THE USAIR CHAIRMAN WASN'T PUSHED

In "Brawl in the cockpit at USAir" (News: Analysis & Commentary, Sept. 25), your writer misrepresented my comments about Seth E. Schofield and the job he has done as chairman. I specifically said that no one on the board encouraged him to retire and that it was his decision alone, with the board ultimately acquiescing. Under Schofield, the company has reduced costs, and his actions played a major role in recent profitability. The job (cost reduction) is only half done. It is up to the workforce to reduce employment costs so we are no longer the highest-cost U.S. car-

rier—if we are to have the long-term ability that Schofield, the board, stockholders, and employees want.

John W. Harris  
President, Harris Group  
Charlotte, N.C.

*Editor's note: Harris is a member of the board of USAir.*

## WHERE IBM STANDS FOR 'I'VE BEEN MISLED'

In "The town IBM left behind," (Special Report, Sept. 11), the author tributes IBM's failure, and the concomitant abandoning of a mammoth chunk of its Hudson Valley manufacturing facilities, to the fact that "its products in many markets were uncompetitive; its rivals simply were better." As a former employee, I beg to differ. The area's manufacturing plants kept competitive through three generations of DRAMS and provided the technology that allowed America to fight back against overseas competition. IBM's laboratories earned the industry's Nobel prizes.

The disaster in the Hudson Valley stems from failure in the boardroom. IBM senior management kept Poughkeepsie, East Fishkill, and Kingsburg churning out mainframes long after the rest of the industry began marching to a different drummer. In the Hudson Valley, the IBM logo really did come to stand for "I've been misled."

Eugene F. Brannan  
Boca Raton, Fla.

## KLAMATH FALLS SHALL RISE AGAIN

I was surprised to find my hometown, Klamath Falls, Ore., mentioned in "Try as they might, the dead seldom rise" (Special Report, Sept. 11). You may be interested to know that Werhauer Co. is alive and well—employing 676 people in the Klamath Falls area. We also have an airport used jointly by the Oregon Air National Guard.

Approximately 45,000 people live

## Business Week

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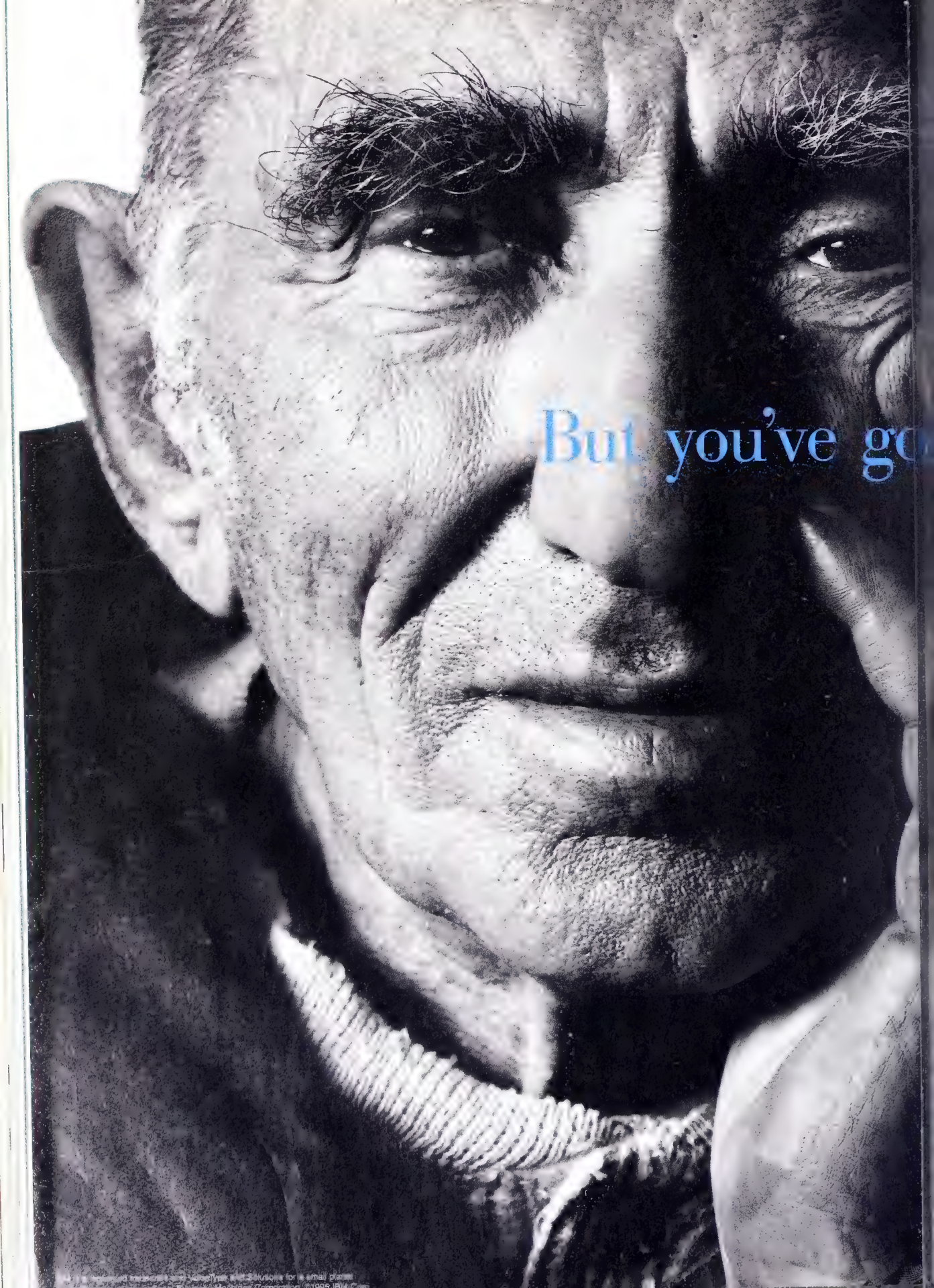


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## Readers Report

### CORRECTIONS & CLARIFICATIONS

"How greed poisoned Pru-Bache," BUSINESS WEEK's Aug. 14 book review of *Serpent on Rock*, by Kurt Eichenwald, stated that Jam J. Darr, the head of Pru-Bache's limited partnership department, "took money under the table from energy and real estate developers." In fact, Eichenwald refers to a financial arrangement with only one developer during Darr's time at Pru-Bache. Eichenwald did not specifically use the term "under the table" to describe Darr's dealings at Pru-Bache. He did, however, provide details of three undisclosed land deals with guaranteed paybacks that Darr received from the sponsor of several limited partnerships he was charged with overseeing. In addition, Darr received a below-market mortgage from a thrift that was part-owned by that same sponsor. Those financial arrangements were also the basis on which BUSINESS WEEK used the term "on the take" in its review of the book.

work in Klamath Falls and its suburbs. Four new operations are in the process of settling into the area: Shilo Industries, International Paper, Sykes Enterprises, and Supply One. To paraphrase Mark Twain: The report of our death has been greatly exaggerated.

Steven V. Hahn  
Executive Vice-President  
Chamber of Commerce  
Klamath Falls, OR

### BINGAMAN AND BLUMENFELD: NO HARD FEELINGS

In "Climbing out of Windows" (Catal Wrapup, Sept. 4), you reported, correctly, that I withdrew from participating in the Antitrust Div.'s investigation of Microsoft Corp. because of a concern about a possible conflict with one of my clients.

You also reported, incorrectly, that I might have had a "falling out" with Anne K. Bingaman. Nothing could be further from the truth. I have only the highest personal and professional regard for Bingaman and for the work she and the Antitrust Div. are doing, including on the Microsoft investigation.

Jeffrey Blumenfeld  
Blumenfeld & Company  
Washington, D.C.

### PG SHOPPING CAN'T MATCH SQUEEZING THE TOMATOES

If online grocery-shopping services such as Peapod ever became viable



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## Readers Report

any doubt that the supermarkets immediately take over this high-in service, at lower costs, and defrom the local store ("The grocery n your PC," Marketing, Sept. 11)? rman's, a Utah grocery chain, set service using America Online last mber. Only 100 people had used it ine, 1995. Why? Except for the wealthy, groceries are a family's st weekly expenditure. If shoppers ot too old or infirm, they want o the roast beef is lean, squeeze matoes, and thump the melons.

William J. Wholey  
President  
Wholey Co.  
Fort Lauderdale, Fla.

### RING A BAILOUT BOTH EYES OPEN

ing unidentified sources, "The new world of Mexican politics" national Business, Aug. 28) incor y reports that a member of the l of Vitro "objected...to Chair- Adrian Sada's plan to spend \$55 n of the company's money to bail oubleunded Banca Serfin, which Sada eads." That never happened. In

fact, board members were upbeat when discussing the opportunity to double Vitro's holdings in Serfin, at 50% of book value.

The story also incorrectly states that Vitro stock took "a hit" when the investment was announced in mid-July. That is not true. In fact, investors reacted positively to the increased earnings in our second-quarter report, in which the Serfin investment was announced.

Raúl Rangel Hinojosa  
President, Legal, Public  
& Corporate Affairs  
Vitro  
Monterrey, Mexico

### READ THIS MAGAZINE AND SAVE \$200

I have subscribed to BUSINESS WEEK for more than 20 years and have found it informative and useful. Most recently, your magazine saved me \$200.

I bought a Compaq computer for my daughter going off to college. Three weeks later, I read "Is Compaq starting a PC price war?" (In Business This Week, Aug. 28), a one-paragraph blurb speculating on whether Compaq Computer Corp. was starting a price war

and saying they had reduced prices.

Armed with that information, I went back to the store to find the price on our model reduced by \$200. This store's policy is for a 30-day price guarantee—and I got a \$200 refund.

Kalman A. Barson  
Bridgewater, N.J.

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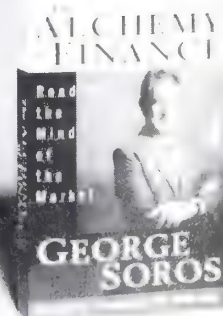
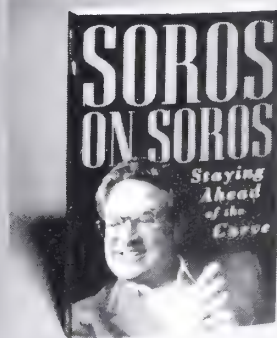
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# STILL TORMENTING THE POWERS THAT BE

At 83, Studs Terkel keeps cranking 'em out. The Chicago radio broadcaster who perfected the form now called "oral history" has published nine books and shows no sign of slowing down—thus epitomizing the main theme in his latest volume. *Coming of Age* is a collection of interviews with Americans over 70, and while not as gripping as Terkel's best efforts, such as *Hard Times*, *Working*, and *The "Good War,"* it is a fine book.

Terkel has always worn his allegiances on his sleeve, a habit that in this book proves both a strength and a weakness. *Coming of Age* is dedicated "to those old ones who still do battle with dragons," and with few exceptions the speakers are battlers—folks who could be resting on their laurels but instead continue to make life hell for the powers that be. What's more, they're all battlers of a certain stripe, leaning to the political left. We hear John Kenneth Galbraith, but not William F. Buckley; we hear veterans of the civil rights movement, but no aging segregationists. The book offers, as Terkel's subtitle announces, "the story of our century by those who've lived it," but it is very much Terkel's take on that story.

At first, I found that take irritating. The book opens with David Brower, founder of Friends of the Earth. At one point he says: "This sounds preachy and that's exactly what it is. I'm a preacher and I make no apologies. You've got to sound off. The older you are, the freer you are, as long as you last." That's a valuable insight. The problem is that Brower and other early speakers often do sound preachy, which turns one off.

But read on, and the book begins to work—the single trumpet note turns into a rich chord. One of Terkel's goals is to recapture America's lost history, to combat what he calls "a national Alzheimer's disease" that obliterates the

memory of injustice and the struggles against it. So his best interviews deliver history as it was made on the picket line and the assembly line, in classrooms and newsrooms and courtrooms.

Gertie Fox, 77, remembers working in a restaurant during the Depression: "The thing that most changed my life was something I saw in the basement of that restaurant—a dreadful thing that bothers me to this day. Why didn't I do something about it? There was a man sitting on the wet floor, peeling potatoes. He was a deaf mute. I made out the paychecks but never made out one to him.... I didn't report it to anyone because I was scared of losing my job." Marvin Miller puts the recent baseball fracas into perspective by recounting how and why the players' union was born. Nebraskan Merle Hansen describes a lifetime of activism in defense of family farmers who "know they're only one mistake away from being totally wiped out." And several interviewees rage against companies and other organizations that dump older workers.

Amid all this boat-rocking, there is little room in the book for oldsters who find more time for play or contemplation. The pleasures of perfecting one's golf game, of surf-fishing on an empty beach—these do not interest Terkel. His subjects talk astonishingly little of relationships with children or with spouses. And as in Betty Friedan's 1993 best-seller *The Fountain of Age*, the dreadful side of growing old—illness, infirmity, looming death—is underplayed.

But *Coming of Age* does resonate with one other great theme: loss. Throughout the book runs a lamenta-

tion, a sense that life in America is getting worse. This might seem a commonplace: Don't old folks always rattle about the good old days? But Terkel speakers see the changes so clearly that their vision seems radical in the best sense of the word. What they pine for can be summed up as the human touch. They remind us that as more and more realms of experience fall under the minion of megacorporations and machines, human contact declines—that the loss is felt in the bones.

Hank Oettinger, a former linotype operator, says newspaper city desks used to be "wild and romantic" places full of bustle and shouting; now they're "dead," the reporters staring at six screens in their cubicles. Painter Jack Lawrence puzzles over students who make computer art: "Hammer? Chisel? Feel the hairs of a brush? They don't want to be accused by their peers of succumbing to this human thing: touch."

Many speakers also lament the fading of the great progressive causes, especially labor, civil rights, and disarmament. Terkel interviews rabble-rousing lawyer Ernie Goodman, 87, in his Detroit office overlooking Cadillac Square, once the site of huge political rallies before the city withered. See Goodman: "See the County Building at the corner of the square? It was built in 1898. There is a stool in front of it, so the person standing on it could exercise free speech. Trying to exercise the right, you'd get arrested as easy as that. After all the battles were over, the stool remained as a symbol: the stool on which you could stand and speak to the masses below. But there are no masses anymore. There's nobody.... In 1950, free speech had a hard time. Now there's plenty of free speech—if you want to address an empty square."

Terkel obviously doesn't believe the square is empty, because he's still on that stool. But *Coming of Age* makes you wonder whether there will ever be another generation of white-haired orators like these.

BY HARRY MAURER  
Maurer's most recent book of interviews is *Sex: An Oral History*.

## Studs Terkel Coming of Age



## TERKEL'S SUBJECTS LEAN TO THE LEFT: WE HEAR GALBRAITH BUT NOT BUCKLEY

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- THE DISCIPLINE OF MARKET LEADERS** by Michael Treacy and Fred Wiersema (Addison-Wesley • \$25) *Consultants diagnose what successful companies do.*
- BUILT TO LAST** by James C. Collins and Jerry I. Porras (HarperBusiness • \$25) *How 3M, Wal-Mart, Procter & Gamble, and others became standouts.*
- HOW TO DRIVE YOUR COMPETITION CRAZY** by Guy Kawasaki (Hyperion • \$22.95) *Pulling off the gloves—and giving the other guy fits.*
- SERPENT ON THE ROCK** by Kurt Eichenwald (HarperBusiness • \$27.50) *How Pru-Bache's limited-partnership deals put the bite on investors.*
- THE BEARDSTOWN LADIES' COMMON-SENSE INVESTMENT GUIDE** by the Beardstown Ladies Investment Club with Leslie Whitaker (Hyperion • \$19.95) *Recipes for Four-Bean Salad, Five-Hour Stew—and 23% returns.*
- THE WARREN BUFFETT WAY** by Robert G. Hagstrom Jr. (Wiley • \$24.95) *A useful analysis of how Buffett does it.*
- THE NORDSTROM WAY** by Robert Spector and Patrick D. McCarthy (Wiley • \$24.95) *A top company salesman describes the retailer's customer-service culture.*
- COMPETING FOR THE FUTURE** by Gary Hamel and C.K. Prahalad (Harvard Business School • \$24.95) *For healthy growth, anticipate the future—and how to dominate it.*
- FIRST THINGS FIRST** by Stephen R. Covey, A. Roger Merrill, and Rebecca R. Merrill (Simon & Schuster • \$23) *Managing your time by balancing your life.*
- MAKE IT SO** by Wess Roberts PhD and Bill Ross (Pocket Books • \$22) *From Star Trek's Captain Jean-Luc Picard, leadership lessons and deep-space lore.*
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- REENGINEERING MANAGEMENT** by James Champy (HarperBusiness • \$25) *Reengineering the Corporation co-author reevaluates.*
- SOROS** by Robert Slater (Irwin • \$25) *The life and investment tactics of "the world's greatest money manager."*
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- 4 **THE WALL STREET JOURNAL GUIDE TO UNDERSTANDING MONEY AND INVESTING** by Kenneth M. Morris and Alan M. Siegel (Fireside • \$13.95) *Concise explanations enriched with graphics.*
- 5 **THE FIFTH DISCIPLINE** by Peter Senge (Currency • \$18.50) *Creating the "learning organization."*
- 6 **1001 WAYS TO REWARD EMPLOYEES** by Bob Nelson (Workman • \$8.95) *Give them a champagne brunch, a casual-dress day—or plain old cash.*
- 7 **THE GOAL** by Eliyahu M. Goldratt (North River Press • \$19.95) *Bringing your strategies in line with your No. 1 purpose: making money.*
- 8 **ZAPP!** by William C. Byham PhD with Jeff Cox (Fawcett • \$10) *How "empowerment" revved up employees at the fictional Normal Co.*
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- 10 **THE REENGINEERING REVOLUTION** by Michael Hammer and Steven A. Stanton (HarperBusiness • \$15) *Roads to reengineering success.*
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BUSINESS WEEK's Best-Seller List is based on a survey of chain and independent booksellers that carry a broad selection of books on economics, management, sales and marketing, small business, investing, personal finance, and careers. Well over 1,000 retail outlets nationwide are represented. Current rankings are based on a weighted analysis of unit sales in August.

## HOT TYPE

When it came to sandbagging the opposition, no one showed more skill than Ben & Jerry's. In a recent contest, A) Richard Nixon, B) Lee Atwater, or C) Ben & Jerry's, the correct answer is clearly C. As a result, Ben & Jerry's faced a potentially crippling threat to its cream distribution network from rival Häagen-Dazs. Ben & Jerry's turned it into a public-relations disaster for that opponent and its parent, Pillsbury Co. Häagen-Dazs had already told a distributor to stop handling Ben & Jerry's or he'd lose Häagen-Dazs' account. Ben & Jerry's responded with a one-man picket of Pillsbury headquarters and bumper stickers reading: "What's the doughboy afraid of?" The low-

budget, David-vs.-Goliath campaign won tons of public support, nationwide press coverage, and ultimately a legal victory.

Kawasaki's *How To Drive Your Competition Crazy: Creating Disruption for Fun and Profit* (Hyperion, \$22.95) includes a number of such tales—other heroes include Honda Motor Co. and Virgin Atlantic Airways Ltd. But this effort by the former Apple Computer Inc. marketing exec and *Macworld* columnist isn't just a collection of anecdotes about leaving the competition in a lather. Instead, the author offers a four-part company-improvement drill that tells how to lay the groundwork, focus on customers, "do things right," and then torment the competition. There's even a section on "how to drive your boss crazy"—complete with tips from a rodeo bull rider.



BY STEPHEN H. WILDSTROM

## ONLINE-AND A BIT OFF THE MARK

**F**or the past several months, the established online services have thought of themselves as Romans facing the barbarians at the gate. Microsoft Corp., a high-tech Alaric the Visigoth, was on the brink of bursting in and stealing their customers.

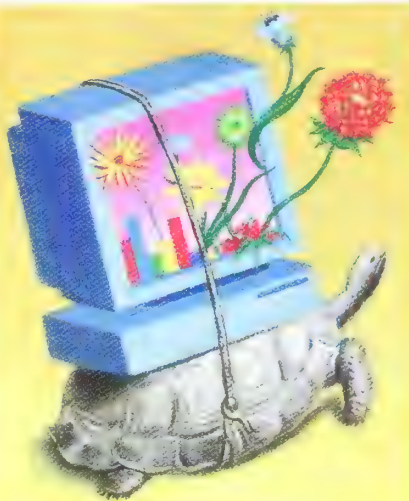
Now that Microsoft Network (MSN) is no longer just a scary rumor, everyone can breathe a bit easier. An early look at MSN reveals that Microsoft's ability to make the service an integral part of Windows 95 is no substitute for the years of online experience enjoyed by its leading competitors, such as CompuServe Inc. and America Online Inc.

MSN feels like a work in progress. I found that its jumble of screens was harder to navigate around than those of competing services. The opening "MSN Today" screen, in particular, gives you no clear indication of what you're supposed to do to find information in the system. The Exchange E-mail program, derived from software designed for corporate mail systems, is awkward and very slow, especially on computers that have just 8 megabytes of RAM. The service makes heavy use of photo-quality graphics. You get some beautiful screens, but you have to spend a lot of idle time online watching those pictures download.

Microsoft won't disclose how many people have signed up to pay \$4.95 a month or \$39.95 for the first year. It

says only that the enrollments are in line with expectations and that the total is fewer than the 500,000 members that the company set as an initial limit.

In one sense, Microsoft has built a network for tomorrow. Borrowing a phrase from hockey great Wayne Gretzky, MSN marketing director Bill Miller says: "We're skating where the puck is going, not



where it has been." But the service has to run on the computers and phone lines of today, and the strain shows. People with fast Internet access, whether through a direct network connection or a digital phone line, will see a dramatic improvement next year. That's when MSN joins CompuServe and AOL in offering access indirectly through the Net.

The problem of content won't be solved so easily. Except for NBC Inc., which provides news, sports, and entertainment, MSN has had trouble lining up high-profile, exclusive-content providers.

For example, only 12 hardware companies, including Dell Computer Corp. and Zenith Data Systems Corp., sponsor forums providing technical support for their products on MSN, compared with dozens on CompuServe. One reason for this, Microsoft officials say, is that many companies involved are concentrating on getting material onto the Internet's Wide World Web.

**NEW GAME PLAN.** The result is a shift in MSN's business strategy that focuses less on exclusive content and more on providing navigational help for Web surfers. "We will add editorial value to the Internet," says Naveen Jain, senior technical marketing manager for MSN.

Many of the most interesting areas reachable through MSN, such as ESPN SportsZone, are just links to the Web. But similar Web links are also available on AOL and Prodigy Services Co. CompuServe will offer access to the Web from its main service before yearend.

The increasing pervasiveness of the Internet might suggest that the days of the proprietary online service may be numbered. But Microsoft clearly does not think so. Neither does AT&T, which has just launched its Interchange Online Network (\$4.95 per month, plus fees for such exclusive services as the *Washington Post's* Digital Ink and computer publisher Ziff-Davis' ZD Net).

For the time being, the commercial services have an important role to play. Information providers have not yet found a practical way to sell a wide range of goods on the Internet, nor have advertisers supported them strongly there. And as a latecomer to the online service business, MSN has a way to go to prove that it's more than just a pretty new face.

## BULLETIN BOARD

### PRINTERS

#### A SHAPELY HP

Hewlett-Packard is taking a plunge into the under-\$500 laser printer market with its new LaserJet 5L. A radical departure from the boxy look of all previous LaserJets, the 5L feeds paper from a vertical bin instead of a tray and prints four pages per minute. A separate slot allows you



feed in envelopes without removing the paper. Using a vertical bin allowed for a less expensive design featuring simpler paper handling and elimination of a fan and other components. Although the 5L increases print quality from 300 to 600 dots per inch, it is expected to retail for around \$480, about \$50 less than the LaserJet 4L it replaces.

### SOFTWARE

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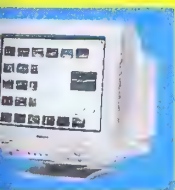
If your work involves math that can't easily be done in a spreadsheet, MathCad 6.0 from MathSoft (617 577-1017) may be the tool for you. Both the Standard (\$129) and programmable Plus (\$349) versions let you do complicated numerical or symbolic calculations on a sort of computerized scratch pad. Results can then be pasted into other Windows applications. While less sophisticated than computer algebra systems such as Wolfram Research's Mathematica, MathCad is much easier to learn and use.

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**Mike Chang, Engineering Manager, Monitor Factory  
Taoyuan, Taiwan**



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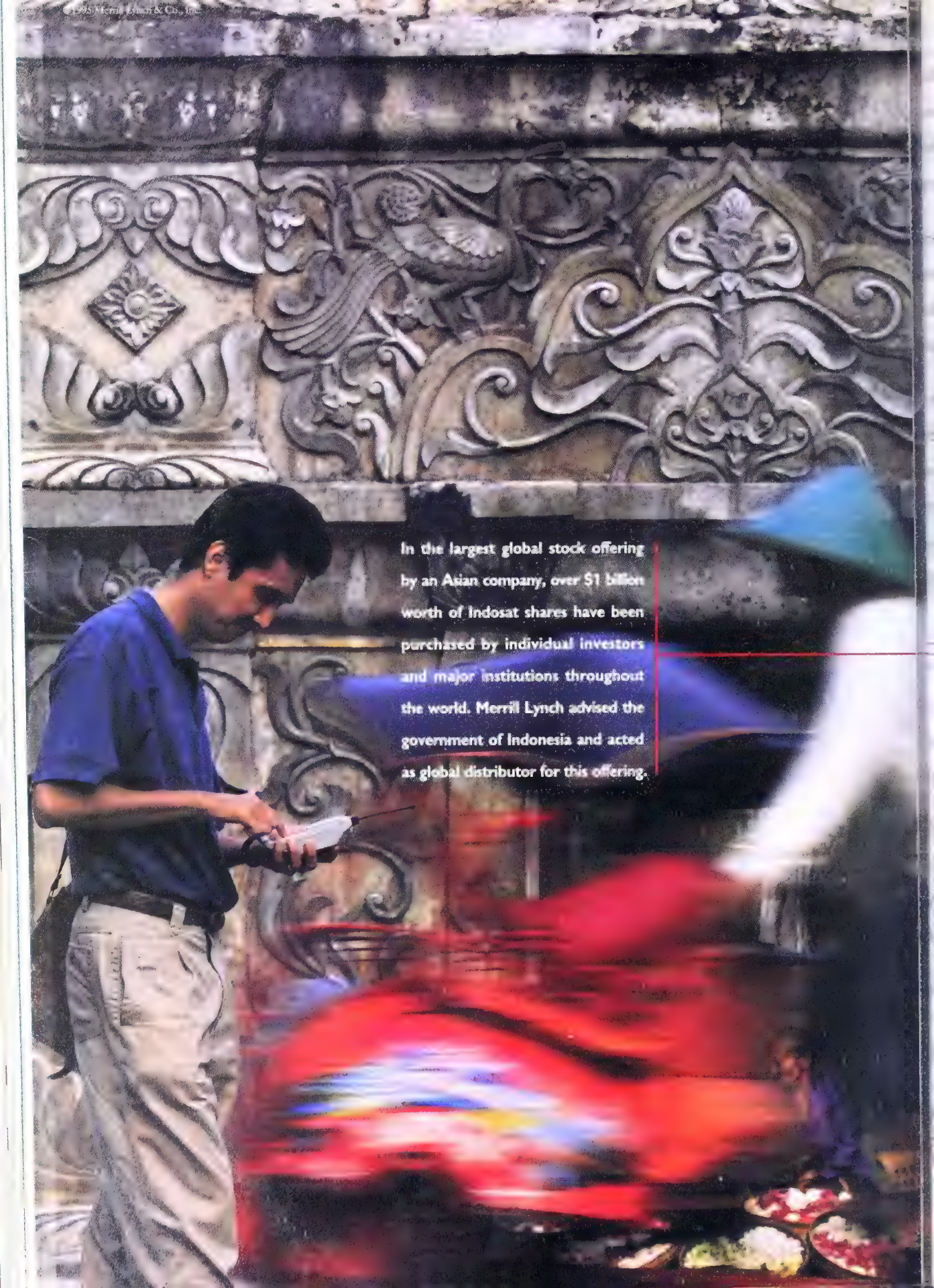


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## THE DIFFERENCE

## BETWEEN STATE OWNERSHIP

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BY ROBERT KUTTNER

## LOOK WHO WANTS TO TINKER WITH MARKET FORCES



### VISIBLE HAND:

By proposing regulation of foreign trade, Pat Buchanan recognizes that workers must be protected from unrestrained capitalism

**P**at Buchanan, the most conservative candidate in the 1996 Presidential field, issued a startling Labor Day statement proposing regulation of foreign trade. Sounding to the left of House Democratic leader Richard A. Gephardt (D-Mo.), Buchanan warned of the "stagnant wages of an alienated working class" and proposed to "insulate the wages of U.S. workers from downward pressure from foreign laborers who must work for \$1 an hour or less."

Unlike his conservative colleagues who insist that markets can do no wrong, Buchanan recognizes that a market is anchored in a national system of laws, rights, and obligations, which defines a political community. Although there are (weak) international laws, there is no transnational sovereign polity and, hence, no meaningful global standards.

In the U.S., slave labor is illegal (though recent reports about Los Angeles garment workers suggest it isn't extinct). There is a right (often breached) to organize unions, to workplace health-and-safety protections, a minimum wage, bans on child labor, and other social "floors" absent in many countries.

To evade these rights and responsibilities, corporations need only relocate in a cheap-labor country. The free-trade dogma insists that trade always improves economic efficiency. But Buchanan and other skeptics note that the costs can sometimes outweigh the benefits by eroding the standards that make our society a decent place to live.

Buchanan would not ban trade. He would, rather, impose a "social tariff" on countries with shabby labor standards, so that their practices would not drag down ours. This would encourage low-wage countries to clean up their acts and would create a buffer to insulate American workers from those that refused. It would also dilute the economic advantage for U.S. companies that exploited cheap foreign labor.

**CRASS COMMERCIALISM.** It is breathtaking to see a conservative embrace a social tariff. But traditional, old-fashioned conservatives, such as the political philosopher Edmund Burke, also worried that market forces, taken to an extreme, would wipe out cherished tradition and social order. In Europe, Christian Democratic parties have long used government programs to shore up family economic security, in the name of traditional values.

We see the lingering conservative ambiva-

lence about markets in the dismay at the violence purveyed by Hollywood, the soft pr of Calvin Klein's fashion ads, the promotion of teenage smoking by Joe Camel, and of assaults on decent values by crass commercialism. Market forces, apparently, can do wrong. When *The Wall Street Journal* editorial page, the very temple of market worship, ran a snide article dismissing the death of Jerry Garcia as a "drugged-up knockoff of a social experiment that went sour," the *Journal* received numerous letters pointing out the contradiction. If millions of fans bought the Grateful Dead's records and went to his concerts, taunted one, then Garcia must be a great musician: "The market proved it. That is, if you believe in markets."

**IDOLATRY.** Recently, Mitt Romney, the entrepreneur and 1994 Massachusetts GOP Senate candidate, stood with President Clinton to decry the Republican attacks on AmeriCorps, Clinton's national service program. Romney, on the board of the City Year volunteer program, thinks service programs revive civic spirit. But among the conservative majority in Congress, market idolatry has reached the point where even government-sponsored programs that promote traditional values are under ideological assault by extremists.

Sometimes, regulations (such as labor standards) and government programs (such as AmeriCorps) can actually shore up old-fashioned virtues of hard work, discipline, and community, while market forces can undermine them. Unregulated trade with low-wage, low-standard countries makes fools out of America's diligent working people. Buchanan observes: "It is mindless to enact health, safety, and environmental laws, wage laws, and family-leave laws, and then via NAFTA and GATT to invite the very companies Congress is regulating to move to Mexico or Asia."

Of course, in proposing social regulation of foreign trade, Buchanan is coy about whether he backs such regulation domestically. However, if he attacks the absence of social standards abroad, he ought to welcome their presence at home. For market forces, left to their own devices, produce intolerable extremes that undermine the domestic order that Buchanan prizes. Buchanan opposes free trade mainly as a nationalist. But if social regulation is good enough for a bunch of foreigners, isn't it also good for American workers?

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'Mrs. Alvarez, how do



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Solutions for a small planet



BY MIKE McNAMEE

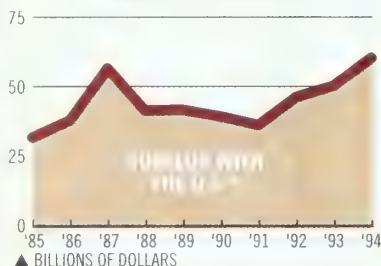
## ASIA'S NEW DRAG ON THE BUCK

The deficit isn't only with Japan

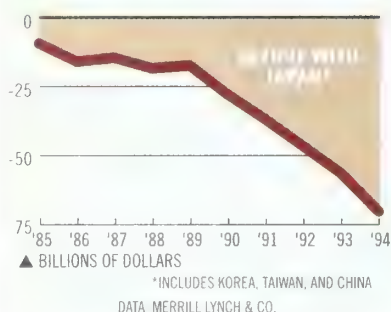
The dollar's recent rebound has some currency mavens boldly predicting that the greenback could soar to 130 yen by next year. But the bulls may be overlooking a persistent pattern in trade flows that weighs down the buoyant buck: America's ballooning trade deficit with Asian countries other than Japan.

While U.S. negotiators have focused on reducing an intractable trade gap with Japan, the deficit with the other

### EAST ASIA: TRADE WITH THE U.S. GAINS...



### ...AS THE GAP WITH JAPAN WIDENS



Asians—primarily China and Taiwan—has soared 50% since the mid-1980s, to \$60 billion. Those countries, in turn, use the dollars they earn to pay for goods bought from Japan. That finances their trade deficit with Tokyo, which has quadrupled to \$80 billion in the past decade. But when Japanese manufacturers get the greenbacks, they quickly sell them for yen. The result of this three-cornered trade tangle: “a Bermuda Triangle for the dollar,” says John Praveen, a Merrill Lynch & Co. international economist.

The U.S. can't easily break out of that cycle. To protect their fledgling exporters, many Asian nations peg their currencies to the dollar—at exchange rates as low as 60% of what some economists consider fair value. They enforce those rates with strict controls on outside capital: Last year, Malaysian officials blunted a speculative effort to drive up the ringgit by limiting the amount of foreign funds banks could keep in interest-bearing accounts and barring locals from selling short-term money instruments to foreigners. Meanwhile, Asian central banks have amassed some of the world's largest war chests of dollar reserves.

The Bush Administration was able to persuade Taiwan and South Korea to revalue their currencies. But Clintonites, focused on trade talks with Japan and sour diplomatic relations with China, haven't tried to square accounts with the other Asians. For the buck, that could spell trouble for years to come.

By Dean Foust

## A HEADSTART FOR KIDS WHO WORK

Peers who don't, earn less later

Educational reformers have fingered the after-school job as a prime culprit in the declining achievement of America's high school students. But whatever damage burger-flipping or gas-pumping may do to a pupil's homework, it appears to pay off in future earnings—especially for students who don't go on to college.

Kids who work during their sophomore, junior, or senior years earn substantially more than their nonworking counterparts six to nine years after graduation, says Christopher J. Ruhm, an economist at the University of North Carolina at Greensboro. Among seniors who never attended college, those who worked 10 hours a week gained 21% over their nonworking classmates. But college-bound workers gained only a 9% earnings edge over nonworking students who also went on to college.

Work had its biggest impact, Ruhm found, in the senior year: Getting a job earlier didn't measurably boost future earnings. The economist speculates that seniors are able to keep working for the same company after graduation—or at least make the school-to-work transition more smoothly than do their nonemployed classmates.

## A QUEBEC LIBRE COULD BE LONELY

Its Canadian trade might be hurt

The U.S. and Canada share the world's most open border and the biggest trade flow—a relationship separatists take comfort from as they argue that Quebec should be a sovereign nation. Campaigning for an Oct. 30 referendum on separation, the Quebecois say the free flow of goods across the U.S.-Canada border is proof that independence would put an economic barrier between Quebec and English-speaking Canada. But a new study from University of British Columbia economist John F. Helliwell throws some cold water on that idea.

While most Canadians believe the economy is tightly integrated with that of the U.S., in fact one province is more likely to trade with another province than with a U.S. state at the same distance, Helliwell found. For Quebec, interprovincial trade is 26 times greater than its cross-border commerce. “Quebec is even more tightly tied to the fabric of Canada than are the Anglophone provinces,” Helliwell writes. That suggests independence could be economically disruptive for both Quebec and Canada's remaining provinces.

## A TORRENT OF TAX BREAKS

States rush to lure companies

The War Between the States is over—it's heating up. Corporate and finance execs say state and local governments are increasingly likely to dangle tax credits and rebates as incentives for companies to expand or relocate operations. In a July survey of 203 companies with gross revenues exceeding \$300 million, accountants KPMG Peat Marwick found that 79% say they're now getting tax breaks. Enterprise zones are popular: 57% of the companies have operations in redevelopment areas where state and local taxes are sharply reduced.

Governments maintain that tax breaks draw in new facilities that create new jobs. But 19% of the surveyed companies say they're getting incentives on current facilities that haven't expanded. How about a tax break, the survey asked, would persuade your company to move its headquarters? Three-fourths of the executives wouldn't answer. But among those who did, the median price tag was \$5 million.



Special Advertising Section

# THE FREQUENT TRAVELER





## THE FREQUENT TRAVELER

# Polished Apple

*An Insider's Guide to New York:  
The Business City That Never Sleeps*



Sony's movie mega-center combines old palaces with spectacular 3-D films.

*Few companies  
can resist  
New York's  
rare mix of  
glamour,  
speed,  
and efficiency.*

“This is the place to be,” Crate & Barrel founder and president Gordon Segal proclaimed at the recent opening of his Manhattan superstore.

The master retailer is hardly the only one saluting New York these days. Walt Disney Chairman Michael Eisner has helped turn the city into a multi-media hub by launching *Pocahontas* in Central Park, investing in a new film showcase that will help 42nd Street clean up its act, and buying the ABC network.

The city the Indians sold for \$24 continues to be America's biggest corporate headquarters town and — thanks to Wall Street — the world's busiest financial center.

Love it, hate it, New York has more than the nine lives of a cat.

Few people — or corporations — can resist its rare combination of glamour, speed, and efficiency.

Now 1995 is shaping up to be the best year for tourist and business travel in this decade — with an estimated 24.8 million visitors. It'll beat 1994 by 200,000.

**WORKSTYLE** When you're visiting, bring along your running shoes — the pace of New York business is grueling. Line up appointments well in advance. New Yorkers aren't unfriendly. They're just busy — or out-of-town (or out of the country). And make sure your credit cards

haven't hit their spending limits. Prices are, on average, the highest in the nation.

**AIRPORT CONNECTIONS** Here are the fares and times to and from midtown (42nd Street) in moderate traffic: **LaGuardia** (\$9 Carey bus, \$20 taxi, 30 to 45 minutes), **JFK** (\$13 Carey bus, \$30 taxi, 60 minutes), **Newark** (\$7 Olympian bus, \$40 taxi, 45 minutes). If you're traveling in a team and on a fast track, phone **National Helicopter** (800/645-3494) and fly over the traffic. Fare: \$299 for a Bell 430 six-seater helicopter, which services all three airports and uses helipads at 34th Street and 60th Street on the East River, 30th Street at the Hudson River, and near the Trade Center downtown.

**HOTEL HITS** New York has more hotel rooms than any other American city except Orlando. Even so, room rates are the highest in the nation, averaging more than \$100 a night. Note that hotels are fullest in October when the fall business season begins and the United Nations is back in session.

In midtown, where many major corporations from Citicorp and Morgan Stanley to Philip Morris and Seagram have head offices, there's a smorgasbord of hotel choices.

■ Want to impress your business contacts? Stay at the prestigious **Plaza** (800/228-3000). It still glitters.



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Our new design is all the rage. But we'd like to point out that beauty is more than paint deep. We've also made a number of other improvements at TWA. Like the new planes we've added to our fleet. Or like our Trans World One<sup>SM</sup> service that offers first class service at a business class fare. Or the new, more convenient flights we've added to our over 80 worldwide destinations. Or our new flights

to Mexico. Or our competitive fares, or the way we've renewed our commitment to customer service. In fact, you might say that we're giving ourselves a makeover. Which is why we say that we're up to something good at TWA.

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## THE FREQUENT TRAVELER

Nations. You're midtown, but the hotel runs complimentary limo service to Wall Street every weekday.

### GETTING AROUND TOWN

Taxis are cheap. For instance, it's only \$3.50, tip included, between Grand Central (42nd Street) and the new and booming Flat Iron District (around 23rd Street), now populated with

advertising and media offices.

Subways are vastly improved, with some redecorated stations and tough rules on panhandling. But if you're a businesswoman, avoid them after about 7 p.m.

**POWERLESS BREAKFASTS** The Big Apple invented the power breakfast, which lives on as the "business breakfast" (7:30 to 9 a.m.). But it's expensive — easily \$15 to \$20 per person.

Go for the place that created it: 540 Park (759-4100), a.k.a. the Regency Hotel. You'll still see Wall Street movers and shakers — without yellow Eighties power ties. Another choice spot, right in Rockefeller Center: the American Festival Cafe (246-6699), below street level at rinkside where skaters swirl during the winter and umbrellas flutter in warmer months.

**'LET'S DO LUNCH'** It's no longer "long" (often only 12:15 to 1:45 p.m. maximum), thanks to Nineties discipline.

Social customs of the natives: New Yorkers are generally on time. They'll readily exchange business cards. And they'll haul out papers and spread them all over the place, even taking notes — except in clubs such as the Harvard, Metropolitan, Union League, and University, which frown on or prohibit workaholic displays.

David Manning loves

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because he's guaran-

teed that Bruce gets his pages.



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The rebuilt Vista looks like new despite the damage from the World Trade Center bombing.



If you're on a budget and picking up the check, steer your guest to places that offer prix fixe business lunches. For instance, **Oceana** (759-5941), a top-tier restaurant where star-chef Rick Bonen produces seafood miracles, has a \$44 three-course lunch. Here are some best picks to put in your little black book (New York area code: 212).

**BEAK ROW** The true-grit **Palm** (687-5533) was the first in the chain — and still the best. **Sparks** (687-4855), wood-paneled and handsome, has tables far apart, helpful for dealmaking. For out-of-town owners, it's a relief to — finally — have **Morton's** (972-3315) and **Ruth's Chris Steak House** (245-9600) in the Big Apple.

**CLASS ACTS** It's elbow-to-elbow with hard chairmen and celebrities at **Le Cirque** (794-9292) where maestro Sirio Maccioni orchestrates the networking. Broadcasters, book publishers, big-time lawyers and advertising whizzes inhabit **Four Seasons** (754-9494 and not to be confused with its hotel namesake) — book the Grill Room at lunch and Pool Room for dinner.

Less expensive but gorgeous with its grand Canal mural, **Remi** (581-4242) serves Italian fare in a dramatic Venetian setting and attracts a lot of magazine editors. The dessert sculptures at the otherwise businesslike **Symphony Cafe** (397-5955) are museum quality. And at the new **Judson Grill** (582-5252) the grilled dishes are as good as the brasserie-style setting. In Downtown (south of 42nd Street), dine at the upscale **Union Square Cafe** (243-0020) if you can't get into the new and currently fashionable **Gramercy Tavern** (777-0777), both featuring fine contemporary American cuisine.

If you're taking a financial tycoon to lunch, your best bet is to book **Bouley** (808-3852), a short walk north of Wall Street.

For a pastoral escape from the city's

*At Le Cirque  
maestro Sirio Maccioni  
orchestrates the networking  
among board chairmen  
and celebrities.*

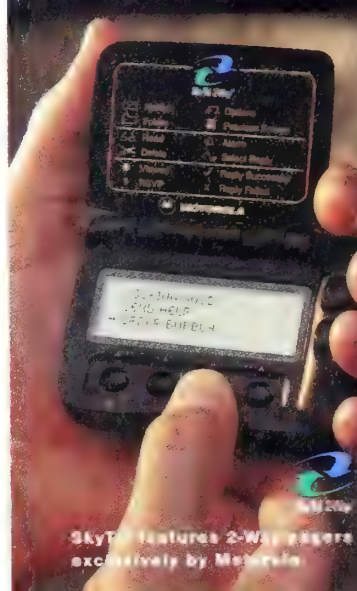
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## WHY DO THEY SCHEDULE MEETINGS FOR 3:00 IN THE MORNING?

*Actually, they don't. It only feels that way when you're jet lagging.*

*Fortunately, relief is now at hand. It's the Hotel Okura's Jet Lag Plan, designed to get you up on your feet and feeling chipper. It includes a Light Box to help put your body's clock back on schedule, a Health Club workout and Jet Bath, Relaxation Videos, a Body Sonic Massage, your choice of pillows to help you sleep better (we'll even remember your favorite for your next visit), and special breakfast and dinner suggestions for extra energy.*

*The Jet Lag Plan is only ¥10,000 extra per day, or free for members of the Okura Club International, our special program for frequent guests. To receive a free brochure, simply mail your name and address to Hotel Okura, Public Relations Office, 2-10-4 Toranomon, Minato-ku, Tokyo 105, Japan, or fax to 3-3582-3707.*

*Hotel Okura*  
T O K Y O

*The Hotel Okura is the flagship hotel of the Hotel Okura Chain, and a member of The Leading Hotels of the World and UTELL International.*

Pothole Jungle, what else but Central Park's — and Hollywood scion and owner Warner LeRoy's — refreshing **Tavern on the Green** (873-3200).

### QUICK AND CONVENIENT

You're practically in Key West at the **Tropica** (867-6767), tucked away in Grand Central Terminal. Another marina is **Docks Oyster Bar** (986-8080) at 40th Street and Third Avenue. Off Times Square you can sprint through a bistro lunch in an animated ambience at **Cafe Un Deux Trois** (354-4148). **Cité** (956-7100), in the Time-Life Building, is a hot spot for steaks and fries, plus free wine with prix fixe dinners — get a table in the no-reservations **Cité Grill** at lunch for a less elaborate meal.

**ETHNIC AND ECLECTIC** For a culinary trip to the Far East, try the most deftly prepared Chinese food in New York at the **Shun Lee Palace** (371-8844) on 55th Street — expensive but smooth as silk, in decor as well as cuisine. Return to the days of the French empire at **Le Colonial** (752-0808), a chic Vietnamese outpost on 57th Street. Aficionados of Indian food with luscious spices pack **Dawat** (355-7555), not cheap but worth it. There's melt-in-your-mouth Kobe beef — and superb sushi — at **Seryna** (980-9393) on 53rd Street.

On the Moscow-to-Marrakech circuit, **Matthew's** (838-4343), which features new American cuisine, lets you relax in an ambience reminiscent of Rick's Cafe in Casablanca. Caviar and vodka, followed by chicken kiev? Of course, the resplendent **Russian Tea Room** (265-0947), next to Carnegie Hall and just bought by restaurateur LeRoy.

**FREE TIME** Visit the Sony movie mega-center — 12 theaters modeled

after historic Loews palaces — at Broadway and 68th Street and see **Wings of Courage**, the first Imax 3-feature film. You wear \$400 headsets as you view the eight-story-high screen, which out-Hollywoods Hollywood.

To see the latest in avant-garde art stylish clothes and creative jewelry — you might even buy something — blitz Soho's shops, located just below Washington Square. For current information and advice on hotels, restaurants, sports events, concerts, and city tours, phone 800/NYC-VISIT (692-84748).

**WATERING HOLES** Meet your business friends for a drink, often easier than booking a lunch. Some standouts: the retro and model-packed **Monkey Bar** (838-2600) in the Hotel Elysees; **P. J. Clarke's** (759-1650) at 55th Street and Third Avenue and the **Oak Bar** (546-5330) two old reliables, and — in the World Financial Center near Wall Street — **Edward Moran Bar & Grill** (945-2255), a blast with thirtysomething brokers and bond traders wringing out the day's tensions.

**NIGHTLIFE** Wacky but wonderful, the **Iridium** (582-2121), near Lincoln Square, is Manhattan's newest and hottest jazz club. At the chrome-plated **Harley Davidson Cafe** (245-6000), on the Avenue of the Americas at 56th Street, it's "hogs" to your right, left, and overhead as you wolf down a burger.

Why not book Rockefeller Center's **Rainbow Room** (632-5100), a restored dinner-and-dance jewel that overlooks Manhattan, or **Rainbow & Stars** (632-1000), its engaging night-club sibling — with Leslie Uggams among its roster of entertainers — for the finale of your New York stopover.

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## THE FREQUENT TRAVELER

# TravelUpdate

### PLANE TO TGV TRAIN

Charles de Gaulle International Airport in Paris now has one of Europe's best plane-train connections for getting to appointments on a business trip. If you're flying into the modernistic airport on Air France (800/237-2747), for example, you can take a moving walkway from Terminal 2C, where you arrive, to an adjacent glass-topped rail station and catch a 160-mile-per-hour,

bullet-nosed TGV train to Lyon (2 hours), France's second largest business center; the French Disneyland (15 minutes) outside Paris, where you may be attending a convention, or even to London (3 hours 15 minutes) through the "Chunnel" under the English Channel. For TGV destinations and fares, phone Rail

Europe at (800/438-7245).



At Charles de Gaulle Airport in Paris you can walk from your Air France jet to a high-speed TGV train in minutes.

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pioneered  
navigating  
systems for  
cars and  
installed  
them in  
Olds 88's and  
Cutlass Cieras.*

### VIDEO-CONFERENCING IN HYATT'S TOKYO TOWER

The high-priced yen isn't dampening the spirits — or expense accounts — of American executives doing business in Tokyo. The Ritz-Carlton (800/241-3333) and Four Seasons (800/332-3442) have opened outposts in the sprawling, frenetic city, which is New York and Washington rolled into one. And now comes the tony Park Hyatt (800/233-1234) with 14 floors atop the 52-story Park Tower skyscraper in Shinjuku, Tokyo's main corporate center (a half-hour taxi ride from the Ginza downtown).

Along with high-tech guest rooms, there's a business center that provides

international videoconferencing with push-button ease. The system, which uses much-touted ISDN (Integrated Services Digital Network) telephone connections, has links with some 100 U.S. cities and more than 60 countries through Kinko's Copy Centers and Sprint. What you see are full-motion color video pictures — with digital sound. You can hold a conference for groups of up to 12 persons in the hotel's private video rooms or for up to 300 people at a breakfast or lunch in one of the larger Hyatt rooms.

The all-inclusive hourly rate for a room setup, and phone line is ¥50,000 (about \$550) for incoming calls and ¥80,000 (around \$880) for outgoing. Contact the hotel's business center directly (3-5323-3410), Kinko's centers or your travel agent to make arrangements.

After your session, retreat to the hotel's Peak Lounge on the 41st floor where you can look out on Tokyo and Mt. Fuji as you sip a cocktail or simply partake of English High Tea.

### FINDING YOUR WAY THROUGH CLOVERLEAFS

"NeverLost" is right on the nose as a code name for the on-board navigation system. Hertz (800/654-3131) has installed in midsize Ford Contours, full-size Tauruses and luxury-class Lincoln Town cars. For the past two months, the high-tech "chauffeur" that helps steer you to business appointments has been available at some rental counters in Atlanta, Chicago, Detroit, Los Angeles, Miami, New York, Orlando, San Francisco and Washington, D.C. And it's first come, first served—no reservations possible. So long as renters take to the system the way they have with rival systems, NeverLost is sure to become an option in other U.S. locations, Canada, and Europe, according to Robert J. Bailey, Hertz senior vice president.

A SEAT SO COMFORTABLE, YOU MAY WANT  
TO REQUEST A WAKE-UP CALL.



*I*NTRODUCING L'ESPACE 127  
BUSINESS CLASS SERVICE



Sleep is a precious commodity in the upper reaches of the atmosphere. Especially when business demands a meeting in Europe early the next morning. Fortunately, Air France's new L'Espace 127 offers business travelers the comfort of a seat more likely found in first class than in business. One that reclines further, replicating the body's natural sleeping position. A seat designed for total muscle relaxation. In your waking hours, L'Espace 127 boasts a built-in video entertainment system, a travel kit with a full complement of amenities, and the finest wines and French cuisine Air France has to offer. For information and reservations, call your travel agent or 1-800-AF PARIS. No, you're not dreaming. Not yet, anyway.

**AIR FRANCE** 



## THE FREQUENT TRAVELER

That's also true for the quite similar navigating systems introduced by its competitors. A pioneer in automatic auto guidance, Avis (800/331-1212) began testing computer-guided Oldsmobile several years ago in Orlando and San Jose, California. Last fall it went on-stream with its Satellite Guidance System and now has around 750 guidance-equipped Olds 88's and Cutlass Cieras for rent in 12 cities: Atlanta, Chicago, Detroit, Indianapolis, Los Angeles, Miami, New York (LaGuardia, JFK, and downtown Manhattan), Orlando, San Francisco, San Jose, Washington, D.C., and West Palm Beach. Spokesperson Terry

Gordon says that Baltimore, Boston, Dallas, and Houston should be coming on-line within the next month or so.

Not to be outdone, National Car Rental (800/328-4567) is trying out its Navigator system in all of the 200 Cadillacs it has in Atlanta and Detroit.

What has delayed the spread of

NeverLost-type systems is the laborious process of mapping an area and loading the information onto a database. But now that Hertz and others have found suppliers to provide computerized road maps, rental cars are a logical choice for testing any navigating system.

### TRIPLE 7 TAKES OFF

When Boeing set out to design its new wide-bodied, long-distance 777 jetliner, it let its airline customers and their passengers come up with the big ideas.

Well, the \$122 million, 292-passenger newcomer is a bird created to provide plenty of creature comforts — a happy thought if you're a frequent business traveler. Exasperated by tight

seating? All the seats on the Triple 7 are roomier than those on most jets — with ample width and pitch (the distance between rows). Tired of banging your head against overhead bins when you deposit or withdraw your carry-ons? The cabin of the Boeing 777 has the look of a wide, high-ceilinged room, partly because bins hug the ceiling — out of the way. Irritated when your overhead light is dim or dead? Built into the plane's design is a computer monitor that warns the cabin staff when accessories need fixing. And there's even a no-roll system for keeping food-and-drink trolleys in place.

As for work-and-play electronic equipment, you'll of course find phones at hand. Personal video screens come out of the armrests in first and business class — and reside in seatbacks in coach. This fall United, the "launch customer," is installing interactive handsets that double as keyboards for playing games and scrolling through shopping catalogs and credit-card phones.

United already is operating the Triple 7 on key business routes: between Chicago and Denver, Washington and Frankfurt, and between Washington and London. Some of the 34 777s the airline has ordered will soon begin servicing other transatlantic city pairs, such as New York and Paris, and flying on Latin American routes.

It won't be long before Boeing's other Triple 7 customers — All Nippon Airways, British Airways, Cathay Pacific, and Japan Airlines, among them — begin operating the jet on numerous domestic and global routes.

### GETTING SET FOR PHONING ABROAD

Cellular phoning is as much an addiction in foreign countries as it is here. Even China now has millions of mobile-phone users. But you can't blithely use your cellular on a trip abroad because of incompatibility with most foreign systems.

One answer is to rent abroad. From The Hague to Hong Kong you can pick up



'Launch customer' United is using the roomy 777 on U.S. and foreign routes.

*Thai-style  
pavilions,  
three-star cuisine,  
elephant rides —  
it's all at the  
Regent's new  
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**RENAISSANCE**  
HOTELS AND RESORTS

cellular at many upscale business hotels — or at the nearest airport when you arrive.

But now both the Baby Bells and entrepreneurs are renting mobile phones for pickup here or at the foreign city you're visiting. You can get your overseas phone number before you step on the plane, and you hit the ground running — and talking — upon arrival.

Typical of the companies providing this service for businesspeople heading for Europe is **Global Cellular Rental Ltd.**, which has a reservation center in New York (800/699-6861) and operations center in London. Rates are £6.95 (about \$10.50) per day; £45 (\$68) per week, and £120 (\$180) per month. If you rent for more than 14 days, there's no charge for delivering or picking up a phone. For shorter rentals, there's a charge of £5.30 (about \$8) if you're in central London and £29 (\$30) elsewhere in Britain or in major cities in the European Union.

Global Cellular Rental, by the way, hooks up with the Vodaphone network, Britain's largest cellular carrier, which in turn uses GSM digital technology throughout Europe — one of three worldwide systems. You obtain your European phone number up to 48 hours before departure. And you get call-forwarding and voice mail at no additional cost. But take note, you can't access toll-free numbers or special AT&T, MCI, or Sprint calling card networks on your cellular.

#### **HOTEL HIGHLIGHTS**

Where you stay helps make your trip pay — particularly if you're trying to impress your business contacts. Some hotel standouts from around the world:

■ The aristocratic but folksy Texan who brought you the Mansion on Turtle Creek in Dallas, London's Lanesborough, Little D Bay on Virgin Gorda, and other luxe establishments — billionaire Caroline Hunt of **Rosewood Hotel & Resorts** (800/928-3000) — has other classy properties for high-level executives on the drawing boards, according to Atef Mankarios, president and chief executive officer. Two are in Saudi Arabia, a country still loaded with oil riches and visiting corporate travelers. Plans are afoot for a Rosewood hotel, combined with a shopping mall and residential structures, next to the **Hotel Alkhozam** in Riyadh. With the muslim country resort-short, Rosewood also plans to open a deluxe, mountain-rimmed getaway at Abha on the Red Sea, only an hour's flight on **Saudi Arabian Airline** (800/472-8342), south of the capital. It should be a welcome escape hatch for American oilmen, construction engineers and other businesspeople. Rosewood's wish list includes a third hotel in — of all places — Sao Paulo, Brazil's biggest business center. Once a kid of urban wallflower, the sprawling city (pop. 21 million) is now developing a higher and more attractive profile, thanks to the booming Brazilian economy, American investments, and the city's unmasked attractions (turn-of-the-century mansions, superior restaurants, red-hot nightlife).

■ For a short break from the sizzling heat and traffic gridlock of Bangkok, Thailand's business hub, fly north to Chiang Mai, near the Burmese border, and spend a few days at the new **Regent Chiang Mai** (800/332-3442). You stay in your very own Thai-style pavilion with peaked-roof outdoor "sala" for d-

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## THE FREQUENT TRAVELER

ing and dreaming — all set in a hillside amphitheater carpeted with rice paddies and tropical flora. The spicy Thai cuisine is three-star, and nearby you can play golf, ride elephants, raft on rivers, and take a Land Rover to see Thai tribesmen and the jewelry, baskets, and clothes they so skillfully craft. The quality experience at Chiang Mai should be no surprise, when you consider that the **Regent** in Hong Kong, the chain's flagship, is one of the world's best hotels.

■ Closer to home, **Sheraton** (800/325-3535), which provides blue-chip accommodations world-wide with its "Luxury Collection," is now offering an enticing

package of full-service facilities and services for cost-conscious business travelers at its new **Four Points Hotels**. For \$70 to \$110, the new establishments feature room service, a free newspaper (delivered to your door), laundry service, and a fitness room, plus a restaurant open for breakfast, lunch, and dinner. "We call it truthful service — a

return to what full service used to mean until some of our competitors started cutting back," says Ann Wilson, vice-president and director of the division. Where are the 50 or so Four Points Hotels? "They're in the suburban minicities that are springing-up around most American cities."

Four of the best: the venerable **Excelsior** (with a huge American clientele) on the **Via Veneto** and the **Grand** (near the central bank and key ministries) in Rome, a city loaded with the headquarters of Italy's many state-owned companies; the opulent **Imperial** in Vienna, rated the world's best hotel in a *Conde Nast Traveler* poll of readers and perfect as a base for checking out potential business deals in Eastern

Europe, and the bouncy, superbly located **Palace** in Madrid — it's close to both major corporate offices and the new Museo Thyssen-Bornemisza that houses the steelmaking Thyssen family's magnificent medieval-to-pop art collection.

### CATERING TO EXECUTIVES FROM DRESDEN TO DALLAS

The German-based **Kempinski** chain (800/426-3135) — with 17 hotels from Beijing to Dallas — makes no secret of its goal of catering to an executive traveler's every need and whim, from high-tech facilities in guest rooms to fully equipped business centers. And the comfort factor gets plenty of attention too. For example, if you're doing business deals in the former East Germany, book a room at the **Taschenbergpalais**, a grand baroque residence at the historic and beautiful Theaterplatz in Dresden. Once the home of Countess Cosel, the Elector of Saxony's mistress, and then destroyed during the fire-bombing of the city in 1945, the hotel just emerged from the ruins after a \$180 million reconstruction. Its conference and meeting rooms are as up-to-date electronically as its rooms, accented with red elm wood, royal blue fabrics and polished black granite, are elegant — each one, of course, equipped with air-conditioning and three phones. If you fly first or business class on **Lufthansa** (800/645-3880) from the U.S. to Germany, you'll get a room upgrade and complimentary early checkin/late checkout at the **Taschenbergpalais** and **Kempinski's** five other German hotels. Opening next spring: the **Kempinski Hotel Furstenhof** in Leipzig, a major manufacturing and trade fair town. And other **Kempinskis** are on the way in Brussels, Jakarta, Warsaw, and, topping them all, Berlin where the chain is meticulously rebuilding the famous **Adlon**, a gathering place for Europe's rich and famous from its opening in 1907 until World War II.



Hertz's NeverLost video screens installed in Contours, Tauruses, and Lincoln Town cars tell drivers exactly where they are.

*Sheraton  
is offering  
full service  
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its 50 new  
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## THE FREQUENT TRAVELER

# In the Laptop of Luxury

## *Notable Notebooks To Take On The Road*

Over the past decade losing weight has been a lot easier for computers than it's been for health-conscious Americans. What began as luggables (15 lbs. and above.) turned into portables or laptops (9 to 14) in the mid-Eighties and then into notebooks (7 to 8) and now, in the mid-Nineties, subnotebooks (4 to 6). And they have the 486 power that's desirable for running Microsoft 95, the new, advanced operating system the computer giant has just introduced.



Texas Instruments is making waves with its Extensa family of notebooks that are faster, lighter, more powerful, and more affordable.

*Today's laptops  
have the 486  
power you  
need to run  
the new  
Microsoft 95  
operating system.*

**LEADING LIGHTS** For computer makers, lightweight portables are today's hot sellers. Packed into their slim

size is as much power and versatility as a desktop computer.

Among the leaders is IBM, which has made its mark with the various models of its ThinkPad — an ingeniously sophisticated machine that was on back order for a long time. Compaq's LTE Elite, plus Contura Aero and Aero, are selling like hot cakes. Toshiba, the one major computer maker that produces only portables, has a huge cheering squad of users who've bought its top-of-the-line Portege and Satellite — and other less expensive models. Apple, a powerhouse with its popular notebooks,

is now offering a new 5300 family of performance PowerBooks. And Texas Instruments is making waves with its favorably reviewed Extensa laptops.

Some well-known names in portable are getting a boost by finding foreign partners. Not long ago, AST, a quality manufacturer, got a legup when Korea's Samsung bought into it. And NEC now has a strong sales network for its Versa line of laptops since its linkup with razzmatazz computer maker Packard Bell.

Beyond that, business travelers have additional options today that didn't even exist a year ago. Hewlett-Packard, better known to computer users for its reliable jet and laser printers, is moving into the notebook market with computer users anticipating a line of similarly reliable machines. And DEC, known for its first-rate technology, recently joined the parade with its HiNote notebooks.

If you buy a subnotebook, expect to pay about \$5,000. By definition it's a slightly lighter machine with an outboard floppy disk drive you can leave behind shed weight and bulk. You'll have to live with a smaller keyboard, but even here the designers are coming up with expanding keyboards such as the "butterfly" IBM model. The bottom line, in any case, is to figure out your work pattern and then buy the machine that fits your needs. That way you get personal productivity for the right price. ■

*The text was written by Paul Burnham Emrey of Emlyn Communications Inc.*

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- 1 ☐ Agriculture 2 ☐ Mining, Construction 3 ☐ Manufacturing, Processing 4 ☐ Wholesale, Retail Trade  
5 ☐ Finance, Insurance, Real Estate 6 ☐ Government 7 ☐ Transportation, Public Utilities  
8 ☐ Service Industries 9 ☐ Other - Please Specify:

#### 2 What is your title?

- A ☐ Chairman of the Board B ☐ President C ☐ Vice President D ☐ Treasurer, Secretary  
E ☐ General Manager F ☐ Division Manager G ☐ Department Manager H ☐ Other Manager  
I ☐ Student J ☐ Other - Please Specify:

#### 3 How many employees in your company worldwide?

- 1 ☐ Under 100 2 ☐ 100-999 3 ☐ 1,000-2499 4 ☐ 2,500 - 4,999 5 ☐ 5,000 - 9,999 6 ☐ 10,000 or more

**BusinessWeek**

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AMES C. COOPER & KATHLEEN MADIGAN

## THE ECONOMY IS HEALTHIER— BUT DON'T EXPECT HANDSPRINGS

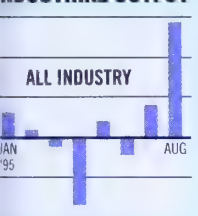
### U.S. ECONOMY

When the Federal Reserve sits down on Sept. 26 to decide where interest rates should be, what will it do? The current betting among economists is that the Fed will do nothing, leaving the federal funds rate on overnight loans between banks unchanged at 5%.

But any decision won't be easy. What the Fed must decide is twofold: How solidly is the economy rebounding, and how restrictive should policy be? So far, the tea leaves strongly suggest that the pickup is only modest and that policy is overly restrictive, given the excellent inflation outlook.

So, a rate cut at the upcoming meeting cannot be ruled out. And even if the Fed stands pat, that doesn't mean that a future rate reduction is out of the picture. With the latest data, which show the economy recovering from its first-half malaise, support that view. In August, strong car buying led a gain in retail sales. Housing starts posted their fifth rise in a row. Industrial production surged (chart). And in July, business inventories grew at their slowest pace of the year.

### BIG BOUNCEBACK IN INDUSTRIAL OUTPUT



MONTHLY PERCENT CHANGE  
DATA: FEDERAL RESERVE, BUSINESS WEEK

Even so, the economy isn't ready to do handsprings. Consumers, while still hanging in there, will not repeat 1994's yearend buying spree. One reason is that they are carrying a lot of new debt now that is becoming harder to pay off. In the second quarter, 1.95% of consumer installment loans were more than 30 days overdue. Delinquencies have risen for three consecutive quarters. At the same time, economic growth, while a bit better in recent months, is slower than it was last year, meaning that incomes will rise with less vigor.

### WHAT IS WHY SPENDING

Spending remains uneven. Retail sales rose 0.6% from July, but excluding cars, store receipts did not grow in either July or August. And the government revised overall July sales down. In terms of gross domestic product, however, consumer spending will contribute to third-quarter growth.

Because outlays began the quarter on such a high level, reflecting strong increases at the close of the second quarter, real consumer spending appears to be rising at an annual rate of 2.5% to 3% this quarter. But that's neither brawny nor broad.

Moreover, households seem a little more cautious. The University of Michigan's preliminary index of consumer sentiment dropped more than seven points in early August, to 88.9, the lowest reading since December, 1993. Early readings on September buying, based on the retailer survey by the Johnson Redbook Service, suggest only moderate retail activity.

The housing rebound needs to be kept in perspective as well. Starts edged higher in August, to an annual rate of 1.40 million from 1.39 million in July (chart). As lower interest rates cleared out some of the inventory of unsold homes, starts have risen 13% since hitting their recent bottom in March, but homebuilding remains below its year-ago level.

Regionally, housing starts since March are up in the Midwest and the West. The South, which accounts for 46% of all starts, contributed nearly 60% of this year's rebound. Starts in the Northeast are below their March level.

In addition, the increase in new mortgage applications to buy a home topped out in mid-July, and have been falling since then. All this means that housing will be an asset for the economy going forward, but the gain will be only a small plus.

Foreign trade, however, remains a minus. The July trade deficit widened further to \$11.5 billion, from \$11.3 billion in June. Imports fell 1.7%, but exports dropped 2.3%. The trade gap began the third quarter wider than its second-quarter reading.

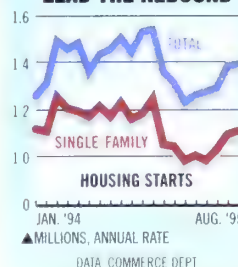
### ONE AREA THE FED

will pay special attention to is manufacturing. Some of Chairman Alan Greenspan's favorite indicators relate to the factory sector, because they often foreshadow turns in the broader economy.

In that regard, the 1.1% jump in industrial production in August is key. Although special factors, including a 4.9% weather-related surge in utility output and a 6.4% bounce in auto and truck production, exaggerated the overall advance, the gain was sturdy and broadly based.

Output in manufacturing alone rose 1%. Even with-

### SINGLE-FAMILY HOMES LEAD THE REBOUND

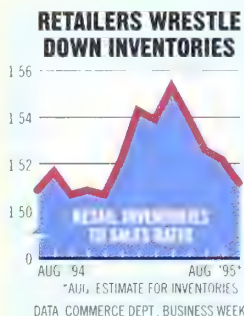


DATA: COMMERCE DEPT.



out the automobile sector, factory production increased an impressive 0.7%, led by gains in business equipment and consumer durables businesses. In the six months prior to August, factory output had either fallen or not grown at all.

Still, August's strong output gain does not look sustainable. First of all, current modest demand growth will not support any more increases that large. Second, now that manufacturers have worked to get their inventories lower, they will be cautious about adding goods in coming months. Inventories held by factories, wholesalers, and retailers rose only 0.3% in July. They had risen an average of 0.6% per month in the second quarter and 1% per month in the first quarter.



The inventory correction, while winding down, is not finished, however. In particular, car output seems to be running somewhat ahead of demand, and retailers may still be in the process of clearing out stockrooms. Their inventories fell 0.7% in July. If the sales jump kept August inventories flat, the ratio of retail sales to inventories likely slipped to 1.51, consistent with the average of this expansion (chart).

However, with consumer demand for goods expected to grow slower than its 3.5% annual pace so far in this upturn, stores may want to start trimming their inventories just a bit more. Slower inventory growth in the third quarter promises to be a substantial drag on GDP growth.

**IN THE FACE OF** what is most likely to be only moderate economic growth heading into 1996, the degree of restrictiveness of Fed policy becomes important. By the Fed's own measure of real interest rates, policy appears to be fairly tight right now.

With the federal funds rate at 5¼%, and with inflation expected to remain at less than 3%, the real funds rate is now a shade over 2¼%. That level is more than one percentage point above the real funds rate's long-term average of 1¼%, which is considered a neutral stance for policy. Above that level, policy is often regarded as restrictive; below that rate, it is accommodative. The Fed has to decide if that level of restrictiveness is warranted.

Moreover, monetary policy cannot ignore fiscal policy. The Fed will probably want to wait and see how much near-term deficit reduction is contained in the 1996 federal budget before sanctioning another drop in rates. But if the budget cuts look credible—and if the economy is no peppier than it is now—look for lower rates by yearend.

## FRANCE

### THE DEFICIT WILL BE TOUGH TO TACKLE

French Prime Minister Alain Juppé has a tough task: to convince financial markets that the 1996 budget he announced on Sept. 20 will trim the central-government deficit from a 1995 target of 322 billion francs (\$63 billion) to 290 billion francs, and that the social security gap will fall by 30 billion francs.

So far, the markets aren't buying it. The government is already overrunning its '95 target by 20 billion francs, making the '96 target that much harder to reach. Plans to tackle the social security deficit are still fuzzy. And the economy is weakening, so the government's annual growth projections of 2.9% this year and 2.8%

next year look unattainable. As a result, investors are demanding an ever-widening premium to own French bonds. The yield on 10-year government bonds on Sept. 20 was 82 basis points greater

than 10-year German bonds.

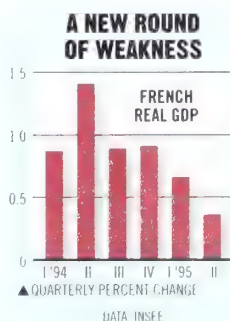
Real GDP in the second quarter rose at a quarterly rate of 0.4%, down from 0.7% in the first quarter and 0.9% in the fourth. Exports have slowed sharply, the result of weaker growth in France's trading partners—notably Britain and Germany. But domestic demand is not taking over as the economy's growth leader, as had been hoped.

More softness is likely. Consumer spending, which surged last

quarter amid a rush to cash in on government sales incentives for cars, is flagging in the third quarter, especially car buying. And the Aug. 1 value-added tax rate hike will hurt spending generally.

Business investment, a key contributor to growth, fell in the second quarter, suggesting that companies are cutting their capital-spending plans. Government demand, which in the second quarter posted the largest increase in nearly three years, will fall off sharply if Paris intends to hold the growth in 1996 outlays at 1.8%, less than the projected 2.2% rate of inflation.

Analysts believe that the ambitious 1996 budget is at least a step in the right direction. And with lower German interest rates likely, the Bank of France has the leeway to cut rates further.



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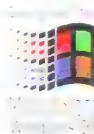
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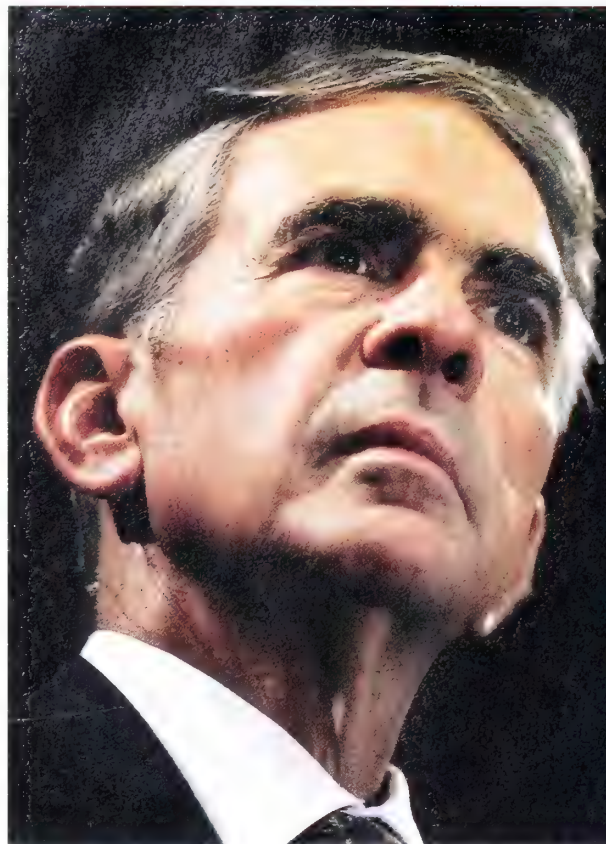
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BREAKUPS

# DIVIDE AND CONQUER?

## Forget synergy. Deregulation means it's time for AT&T to break up

**F**or 100 years, AT&T believed in one thing above all: That bigger is better. It spent decades buying up local phone companies to create the Bell System and then fought off various government efforts to break up its monopoly. Even when Ma Bell was finally dismantled in 1984, AT&T hung on to its equipment-manufacturing business—despite initial opposition from the Justice Dept. Post-breakup, the company continued its buying spree. Under Chief Executive Robert E. Allen, who took over in 1988, the company pulled off two of the biggest deals in high-tech history—paying \$7.4 billion for computer maker NCR Corp. in 1991 and \$12.6 billion for cellular-phone operator McCaw Cellular Communications Inc. in 1994.

Then, early this year, Allen changed his mind. With no signs that the massive combination of technology assets would pay off—and with AT&T's stock stuck in the doldrums—Allen concluded that big isn't necessarily good after all, synergy is dead, and the concept of converging communications and computer markets, which drove the NCR deal, is an illusion.

Now, in an effort to untangle itself, AT&T is engineering one of the biggest voluntary restructurings in corporate history. "We reached a time when the advantage of integration was outweighed by the disadvantage of complexity," says Allen.

**"GUTSY MOVE."** To recover, Allen has moved quickly. In April, he and John D. Zeglis, general counsel, and Chief Financial Officer Richard W. Miller met with investment bankers at Morgan Stanley & Co. and outside lawyers to develop the breakup. The proposal was presented to the board and senior executives in early September during an annual three-day getaway at the Greenbriar resort in West Virginia. Allen says directors agreed to go along with his plan after he promised that he would

**SPLITSVILLE:** Allen is getting kudos for his decision to restructure

stay on as CEO of the largest remaining unit through the transition.

On Sept. 20, the company announced the breakup. The surviving AT&T will include the core \$53 billion long-distance and cellular-phone businesses. The Network Systems Div.—the former Western Electric, which makes the switching equipment used by local- and long-distance companies—will be spun out to shareholders. Allen says AT&T may sell 15% in a public offering as early as the first quarter of 1996. Global Information Solutions, the loss-plagued former NCR unit, also will be spun off to shareholders. "This is certainly a very strong and gutsy move on Allen's part," says John Haigh, a vice-president with Boston consulting firm Mercer Management.

Indeed, Allen, 60, is being hailed as the conquering hero for his very public about-face. AT&T shares took off immediately on the news and soared by nearly 6% to close at 63%. In a matter of hours, that added nearly \$11 billion in value to the company's market capitalization—more than enough to make up for the

The move created more stockholder value in a single day





*To be more competitive in a deregulated phone business—and to boost its stock price—AT&T will split into three separate entities:*

**AT&T SERVICES** The big enchilada. AT&T holds a commanding 60% of the U.S. long-distance business, the former McCaw Cellular owns the largest U.S. cellular network, and its global expansion makes it the largest international phone company in the world. Now, the unit is poised to enter local service—with the best-known brand name in the business. The company would have to work very hard to turn this business into a dog.

1996 REVENUES

**\$53.3\***  
BILLION

NUES

5\*  
ON

and local calling. By spinning equipment into a company, AT&T stands a better chance of keeping its important customers.

**AT&T NETWORK EQUIPMENT** The second-largest telecom equipment maker in the world, with hefty 40% operating margins. But deregulation in the U.S. will pit AT&T against the Baby Bells and GTE in long-



1996 REVENUES

**\$8.3\***  
BILLION

**AT&T GLOBAL INFORMATION SYSTEMS** The problem child. AT&T bought the former NCR for \$7.4 billion four years ago, then watched it sink. The unit has lost \$3 billion since the merger and is now dropping out of the personal-computer business. It also is in for a major downsizing—8,500 of 43,000 jobs will be eliminated. One potential bright spot: The innovative data-warehousing technology NCR bought from Teradata.

\*Estimate

DATA: LEHMAN BROTHERS

purchase of NCR and ensuing losses. "It allows AT&T to rest for its NCR acquisition, which has turned out quite as originally envisioned," says a senior official at Teachers Insurance & Annuity Association-College Retirement Equities Fund, one of AT&T's largest shareholders. "Now, AT&T management can concentrate its energy predominantly on global telecommunications—their area of greatest experience and potential."

Allen has more in mind than refocusing management, though. More than anything else, AT&T's new structure is meant to capitalize on the soon-to-be-deregulated U.S. telecommunications market. Congress is poised to pass a law that will allow local phone companies, long-distance carriers, and cable-TV providers into each other's business. Not only will Allen face the seven well-entrenched Baby Bell regional phone giants in the long-distance business, but he also risks losing them as customers for network equipment sales. The Bells now account for some 40% of the \$23 billion in switches, cable, and other network equipment that AT&T sells.

But the local phone companies, al-

ready leery of throwing this lucrative business to AT&T, are loath to continue buying from the company once they move into long-distance and AT&T edges into local calling. "There has always been a cloud in dealing with AT&T," says Robert L. Barada, Pacific Telesis Group's strategy head. "It makes you stop and think when you buy one of their [fiber-optic cable rings], because you know they're installing the same fiber ring in our territory to compete with us. This will take part of that cloud away."

**TAG TEAM.** Allen concedes that there was a looming problem with the Bells. "These fears and concerns were in part generated by emotions, and they've existed ever since the breakup, but recently they have started affecting our business," he says. How much? Analysts figure that AT&T is losing some \$3 billion in orders each year as a result of that fear. Now, Allen says, the equipment sales force is unleashed. "As wild as it might seem, MCI might buy equipment from something that once was the AT&T equipment company," he says.

The breakup could also let AT&T move more effectively into new markets such

as information networks. "The unbundling is going to make their strategy on things like the Internet better, not worse, because now they could buy from, say, Sun instead of NCR," says Howard Anderson, president of the Yankee Group, a consulting firm. Competitors like that idea: "Hopefully, AT&T Communications will eventually become a good customer," says Northern Telecom Chief Operating Officer John A. Roth. Allen says that AT&T, the long-distance company, will continue to partner with AT&T, the equipment company. The two, he says, have already agreed to pursue the huge Chinese market together.

Another major benefit, says Allen: uncovering the "buried" value of hot-growth businesses such as cellular calling in a stock that has been dragged down by the money-losing computer business. "Without GIS dragging the stock down, the full val-

ue of wireless can be better reflected in the stock price," says a McCaw spokesman. Robert B. Morris III, a Goldman, Sachs & Co. analyst, calculates that the values of the three separate companies, gauged by the multiples of comparable companies—would produce a combined share price in the \$64-to-\$76 range.

For rivals, AT&T's breakup means years of rethinking strategy. Suddenly, they no longer face a sclerotic, confused mass of conflicting businesses. Instead, they must deal with a highly focused and enormously powerful rival in every telecommunications market. "I'm more fearful for ourselves and the traditional telephone-service providers than ever," says Pactel's Barada. "You're talking about a company that will be totally focused on communication services without the distractions of the equipment business or NCR. They're going to really be coming at us to eat our lunch if they get a chance." That's the idea.

*By Catherine Arnst, with Leah Nathans Spiro, in New York, Peter Burrows in San Francisco, and bureau reports*

AT&T's computer division lost in the past 10 years



## LEGAL BATTLES

# THE STORY BEHIND THE BANKERS TRUST STORY

How an investigative piece set off a classic battle over First Amendment rights

**O**n the evening of Sept. 13, just three hours before BUSINESS WEEK closed its issue dated Sept. 25, the fax machine on the 48th floor of the magazine's publisher, The McGraw-Hill Companies, began to hum. McGraw-Hill General Counsel Kenneth M. Vittor was finishing a routine prepublication legal review of an investigative article about litigation between Procter & Gamble Co. and Bankers Trust Co. What emerged from the machine at 6 p.m. dramatically altered the course of the evening. It was not just a court order prohibiting BUSINESS WEEK from publishing information in the article—it was an order that would set off a scramble within McGraw-Hill and at media organizations across the U.S. and set the stage for a test of First Amendment rights.

The issue: The warring companies seemed to have persuaded a federal judge to issue a "prior restraint" of the piece. Bankers Trust has argued that information in the story was taken from sealed court records obtained by BUSINESS WEEK and that it would suffer "irreparable harm" if the information be-

came public. McGraw-Hill, which wasn't given a chance to argue its side before the order was issued, immediately cast the decision as a blatant violation of its constitutional rights under the First Amendment.

After reading the fax, Vittor, who was warned that he would be personally held in contempt if BUSINESS WEEK violated the order, mobilized a team of lawyers in Cincinnati, where the companies' dispute is unfolding. Within an hour, they attempted to contact U.S. District Court Judge John Feikens, who had signed the order. Unable to locate him, the lawyers called Judge Danny J. Boggs of the Court of Appeals for the Sixth Circuit at his home in Louisville. With the magazine's deadline fast approaching, BUSINESS WEEK's counsel implored the judge to vacate the lower court's order. But Boggs declined to take action.

**CHILL FACTOR.** His "no" was an extraordinary blow to the magazine. For the first time in its 66-year history, BUSINESS WEEK was forced by the government to pull a story from its publication. "If this order stands, for no compelling reason,

it reverses at least 25 years of precedent governing prior restraint," says Stephen B. Shepard, BUSINESS WEEK editor-in-chief. "It's really censorship."

The courts' actions also set in motion a legal drama that eventually reached all the way to the Supreme Court and could reshape First Amendment law. At issue: freedom of the press vs. the sanctity of the court system. BUSINESS WEEK maintains that if Procter & Gamble and Bankers Trust prevail, the ability of the media to gather and publish sensitive information could be curtailed. With that argument in hand, McGraw-Hill on Sept. 14 filed an emergency request with the Sixth Circuit appellate court seeking relief from what it believed was a classic case of unconstitutional prior restraint. "The image of judges issuing prior restraints out of their chambers with fax machines, without prior notice to the media, is deeply troubling from a First Amendment perspective," says Vittor. McGraw-Hill has received official support for its position from major media organizations, including The New York Times, Time Warner, Dow Jones

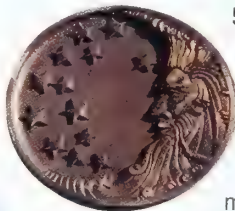
## A Journey to the Supreme Court

SEPTEMBER 13



**5 p.m.:** BUSINESS WEEK editors finalize an investigative article about a legal battle between Bankers Trust and Procter & Gamble. The battle concerns losses suffered by P&G in derivatives

transactions. Information in the story was derived from sealed court documents legally obtained by the magazine.



**5:45 p.m.:** Federal judge John Feikens, who is overseeing the Bankers Trust/P&G litigation, signs an order prohibiting the magazine from publishing any information

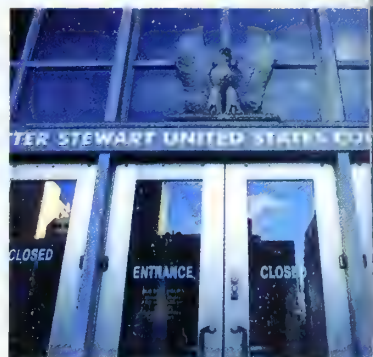
taken from the sealed documents.

**6 p.m.:** Feikens' order is faxed to BUSINESS WEEK.

**8 p.m.:** McGraw-Hill lawyers, unable to locate Feikens, ask an appellate court judge to lift the order, arguing that it is an unconstitutional violation of the First Amendment.

**9 p.m.:** The judge declines to take action. Facing an imminent publishing deadline, BUSINESS WEEK is forced to pull the article from the magazine.

SEPTEMBER 14



McGraw-Hill files an appeal of Feikens' order. It also files two emergency motions with the U.S. Court of Appeals for the Sixth Circuit (above), one seeking to overturn Feikens' order and another asking for expedited appeal of the matter.



Case No. C-1-94-735  
(Judge Feikens)

IES CORPORATION,  
Defendants.

THE PROCTER & GAMBLE  
COMPANY'S MOTION FOR  
LEAVE TO AMEND THE  
COMPLAINT

Defendants.

1. The Procter & Gamble Company ("P&G"), hereby moves this Court for Fed. R. Civ. P. 15(a) for leave to amend its Complaint to assert claims arising out of the Organized Crime Control Act of 1970 (18 U.S.C. section 1961 et seq.) and IX of the Organized Crime Control Act of 1970 (18 U.S.C. section 1962 et seq.). This motion is supported by the Memorandum in Support filed herewith (the "Memorandum").

2. The proposed Second Amended Complaint and RICO Case Statement (including attachments) are appended thereto as Attachments A & B.

court orders barring the publication of news articles have been issued in the past by lower courts. Usually, they deal with national security, trade secrets, a right to a fair trial, or the identity of victims. But the U.S. Supreme Court has never sustained such an order. In its appeals, McGraw-Hill cited several such instances, including the Pentagon Papers case against *The New York Times*. *BUSINESS WEEK's* case focuses on the dispute between two publicly owned corporations—not on the location of the war going to war. "There's no national interest here, just commercial issues,"

Victor A. Kovner, a First Amendment lawyer representing BUSINESS K. Still, says Shepard, the magazine never considered ignoring the order. "We're not above the law," he says. The crux of Bankers Trust's position: The court must be able to enforce its orders. The bank, which is being

## BANKERS TRUST

sued by P&G for \$195.5 million in damages relating to derivatives transactions, contends that preserving the court's power outweighs First Amendment arguments.

**PROMISE OF PRIVACY.** As is the case in many legal battles, much of the fight between Bankers Trust and P&G had been kept under wraps since January 1995, when a court order sealed all discovery material designated by either party as confidential. And even though P&G on Sept. 1 filed a public motion in U.S. District Court seeking to add racketeering charges to its earlier allegations, documents filed to support that motion were sealed. "BUSINESS WEEK has no conceivable right to possess—or even to view—the materials, much less to publish them," Bankers Trust told the appellate court. The bank states that "tens of thousands of sensitive internal documents" were exchanged between the parties based on the promise that they would be kept private. To allow BUSINESS WEEK to now use those

materials in an article, the bank argues, would undermine the power of the courts to control their own proceedings. "The public interest in the smooth and effective working of discovery and in the enforcement of court orders will be irreparably harmed if BUSINESS WEEK is permitted to flout the district court's protective order," the bank told the court in its brief. The magazine says its reporter obtained the document legally and did not know it was under seal.

P&G, which supported Feikens' restraining order, has taken a backseat in the current brawl. "This is not our fight," says a company spokesman. "The materials at issue are not P&G's, they are Bankers Trust's." The spokesman adds that the company supported Feikens' action "to preserve the integrity of the court's protective order."

After a nearly round-the-clock vigil at the Cincinnati courthouse by McGraw-Hill lawyers, a three-judge panel of the appellate court on Sept. 15 was named to hear the case on Sept. 18. Meanwhile, access to information about the case suddenly dried up. Of the thousands of public documents filed in the Bankers Trust-P&G case, not one page could be obtained by reporters. Even innocuous public records, such as the court docket, were unavailable. "We're not supposed to give it out," a clerk told BUSINESS WEEK Cleveland Bureau Chief Zachary Schiller on Sept. 15.

McGraw-Hill hoped it would win the green light it needed to publish its controversial story on Monday, the day of the hearing. But the appellate court

ge appellate court panel is  
hear McGraw-Hill's motion on  
Bankers Trust urges the court  
Feikens' order, contending that  
"irreparably harmed" if the con-  
firmation is publicly disclosed.

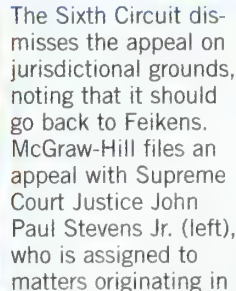


Numerous media organizations, including The New York Times, Dow Jones, Bloomberg, and the Magazine Publishers of America file *amicus* briefs with the appellate court, supporting BUSINESS WEEK's First Amendment arguments. Bankers

Trust asks the district court to issue a permanent injunction against McGraw-Hill. The three appellate judges hold a 50-minute hearing. Most of the session is spent on concerns relating to jurisdictional issues, not on the merits of the case.

**FEDERAL JUDGE FEIKENS:**

*His restraining order galvanized a Who's Who of the media biz*

**SEPTEMBER 19**

the Sixth Circuit. Feikens sets a hearing of his own on Sept. 21 at 9 a.m.

**SEPTEMBER 20**

As BUSINESS WEEK goes to press, Justice Stevens has not ruled on McGraw-Hill's appeal. McGraw-Hill's lawyers continue to press their case.



judges—Robert Krupansky, Alan Norris, and Richard Suhrheinrich—asked 50 minutes of unrelenting questions focused less on the substantive legal issues at stake than on jurisdiction. Why, they asked, had neither party gone back to Feikens to argue the case? “Because of the time constraints, the rules of evidence and practice and procedure be damned,” blasted Krupan-

sky. The next morning, the panel unanimously dismissed the appeal, sending it back to the district court and keeping in place Feikens’ ban.

On Sept. 19, McGraw-Hill upped the ante. The company filed an appeal with Supreme Court Justice John Paul Stevens, the judge assigned to hear appeals of cases originating in the Sixth Circuit. “There is quite literally no sup-

port in this case for the proposition that the prior restraint test has been met,” McGraw-Hill told the high court.

AS BUSINESS WEEK went to press, Stevens had not ruled on McGraw-Hill’s appeal. The scramble continued.

By Linda Himmelstein in New York with Zachary Schiller and Stephen Baker in Cincinnati, and bureaurports

## COMMENTARY

By Catherine Yang

### A DISTURBING TREND TOWARD SECRECY

**T**he trend toward secrecy in litigation is becoming all too routine. One recent example: On Sept. 8, General Motors Corp. settled four cases, at a U. S. court in Oklahoma City, about crashes involving its pickup trucks. But GM and the alleged victims agreed to keep the deals confidential. While GM declined to comment, plaintiffs’ attorneys say the company can count on secrecy to contain potential payouts in 50 similar pending cases.

Companies such as GM often prefer to keep their litigation under wraps. And judges can make it easy—agreeing to requests to keep confidential everything from potentially damning evidence to sealed court filings—which is what’s at issue in the dispute involving BUSINESS WEEK, Bankers Trust, and Procter & Gamble. While legal experts say there are no hard numbers measuring the trend, anecdotal evidence suggests that hushed settlements and protective orders for ongoing litigation are commonplace enough to be troubling.

**A HIGH PRICE.** The use of secrecy “has gotten worse and worse,” says Miami attorney Richard J. Ovelmen, who has defended the right to access for *The Miami Herald*. “It’s an attempt by very rich and powerful litigants to convert the public judicial system into a private dispute mechanism.” Before the drift toward secrecy gets out of hand, judges, lawmakers, and attorneys need to better balance the conflicting rights of corporations and the public.

Companies, of course, have many

legitimate reasons for wanting confidentiality, including the protection of privacy and trade secrets. And judges have great leeway to grant their requests for such “good cause.” Furthermore, just because companies often choose to settle with complainants rather than fight costly legal battles, say defense lawyers, doesn’t mean they must then disclose the de-



tails. “If you got sued for something you thought was totally unfounded, what business is that of the public?” asks Washington attorney Alfred W. Cortese, who has worked for GM.

But in some cases, the public pays too high a price for closed-door deals. For one thing, investors and consumers need to know about complaints against a company’s operations or products. Sealed deals can blot out new information about allegedly harmful products and put consumers at risk. Confidential settlements in 1985 and 1991 between Dow Corning Corp. and silicone breast-implant users shielded documents showing that

the company may have known about its product’s potential problems as early as the mid-1970s, says Dan Bolton, the San Francisco attorney who brought both of those cases. Dow Corning had no comment.

**EXPEDIENCE.** The press, too, shares the need for openness in its duty to uncover corporate wrongdoing or questionable government activities. To perform its role, the media should normally have access to legal documents that shed light on matters that citizens in a democracy have a right to know about.

Yet there’s strong momentum toward secrecy. Plaintiffs often will agree to a secret deal to get higher compensation from companies that want the whole mess kept under lock and key. Judges let these settlements go forward because resolving cases helps clear their overcrowded dockets.

“Everyone’s interest is satisfied except that of the public,” says Arthur H. Bryant, executive director of Trial Lawyers for Public Justice in Washington.

Courts, legislatures, and lawyers need to exercise more vigilance against the secrecy trend. Judges should give greater weight to the public interest in decisions to grant confidentiality requests, and plaintiffs should stand up to pressures to settle in private. Otherwise, the public can be shortchanged by a judicial system they pay for but which doesn’t always protect them.

Yang reports on legal affairs from BUSINESS WEEK’s Washington bureau.



# THE GLOVES ARE COMING OFF AT CHRYSLER

...ome York is preparing a full-scale assault on management

...s head of Chrysler Corp.'s Mexican operations in the early 1980s, ...me B. York would ... local dealerships alone ... weekends, looking for ... ly built K-cars. When ... und one, York bought ... d drove it back to the ... ry to show workers ... re they had failed. ... in 24 hours, all 5,000 ... oyes in Mexico knew," ... says. "It sent shock ... es through the troops."

...rk, 57, spent 14 years ... hrysler shaking things ... s an aggressive, whip- ... t engineer. By the time ... ft for IBM in 1993, he ... risen to chief financial ... er and had built a repu- ... n as a driven loner and ... nding cost-cutter, the ... of executive who en- ... keeping secrets and ... gging surprises.

...ow, as billionaire inves- ... Kirk Kerkorian's new

...-hand man, York is ready to spring ... y surprises on his former colleagues ... hrysler. While he will say little pub- ... about his plans to boost the value of ... orian's 13.6% stake in the carmaker, ... is readying a full-scale assault to ... n within a month, according to ... ces familiar with his strategy. His ... to join Chrysler's board, oust hostile ... ctors, and prod the auto maker to ... as much as \$2 billion of its \$6.9 ... n cash reserve into a stock-buyback ... ram. Ultimately, say associates, York



**YORK:** Eyeing Chrysler Chairman Eaton's job?

... has his sights set on dethroning Chrysler Chairman Robert J. Eaton.

To pull that off, York is expected to orchestrate a chorus of criticism of Eaton's management style and the company's uneven record of vehicle quality. If York can undermine Eaton with powerful institutional shareholders, he stands a better chance of winning a proxy solicitation battle to accomplish at least some of his goals. Says a source close to Kerkorian's Tracinda Corp. investment firm, where York was named

vice-chairman on Sept. 5: "The gloves will come off" soon.

It's a long-shot strategy. Tossing out Eaton would be a tough sell to institutional shareholders: They have been wowed by Chrysler's stellar financial and sales performance under Eaton, who succeeded Lee A. Iacocca as chairman in 1993. Indeed, Chrysler shares are up more than 40% since April. Even investor Robert Day, the Trust Co. of the West leader who was a catalyst behind Kerkorian's first run at Chrysler, is backing away from the Tracinda camp. Day recently sent Eaton a letter informing him that TCW is no longer aligned with Kerkorian.

But after being soundly beaten in his \$20.5 billion takeover attempt last April, Kerkorian seems willing to fight long odds. Kerkorian resents how Eaton strong-armed banks into shunning Tracinda's buyout offer and believes that Eaton misled him about how Chrysler would respond to the deal. "What does Kirk Kerkorian want? He wants Bob Eaton gone," says one Wall Street analyst.

**HIT LIST.** To reach that endgame, Kerkorian and York are gunning for several influential Chrysler directors. Their likely targets: former Kmart Chairman Joseph E. Antonini, former Carter Cabinet secretary Joseph A. Califano, and retired Boeing Vice-Chairman Malcolm T. Stamper. The three infuriated Iacocca, Kerkorian's friend and paid consultant, by forcing him to retire as chairman at the end of 1992. The probable hit list also includes Chrysler Vice-Chairman Thomas Denomme, Eaton's agent in talks with Tracinda last spring.

Even while Tracinda wrestles with Chrysler's board, York will be nagging Eaton to free up cash. Under pressure from Kerkorian, Chrysler has already doubled its dividend, to \$2 a share, since late last year and instituted \$2 billion in stock buybacks. Rumors spread on Sept. 19 that Chrysler would keep cash away from Kerkorian by buying Volvo, but a source close to the Swedish carmaker says the companies have only discussed

## YORK VS. CHRYSLER

...he Tracinda ... ce-chairman's ... probable ... ame plan

### BOUST DIRECTORS

Boot hostile directors. Possible targets: former Kmart Chairman Joseph Antonini, former HEW Secretary Joseph Califano, retired Boeing Vice-Chairman Malcolm Stamper, and Chrysler Vice-Chairman Thomas Denomme.

### GET A SEAT

Win an insider's role by attempting to replace one of the deposed board members with a Tracinda representative, likely York himself. This would probably be accomplished via a consent solicitation of the auto maker's large institutional investors.

### TRASH EATON

To weaken Chrysler's management, Tracinda executives are quietly attacking Chrysler Chairman Robert Eaton's leadership style. York's prime focus: Chrysler's spotty record on vehicle quality.

### CUT CASH

To build support with shareholders, York wants Chrysler to reduce its cash reserves to \$5 billion from its current \$6.9 billion, shifting the extra money to a stock buyback program.



a joint venture. Eaton, to be sure, has been loath to further carve up the cash reserves he believes Chrysler needs to develop new products in the next sales downturn.

But York isn't buying that argument. Neither does he buy into Eaton's emphasis on corporate teamwork. A West Point graduate and disciple of Iacocca's top-down, chain-of-command style, York subtly intimates that Chrysler could flourish better under tighter rule. "The business purpose of teamwork is to produce results, not to create teamwork for its own sake," York says.

**WEIGHING MOVES.** York is soft-pedaling criticism of Eaton's results for now. And he lauds Chrysler President Robert A. Lutz, suggesting the board let him stay on as chief operating officer after he turns 65 in 1997. But in conversations with investors, other Kerkorian operatives are quietly calling Eaton an "indecisive" leader who doesn't push hard enough to improve Chrysler's lagging auto quality, say Wall Streeters.

Still treading lightly, York accepted Eaton's refusal to meet with him, settling for a standard, state-of-the-company presentation on Sept. 19 from a Chrysler team headed by CFO Gary C. Valade. If his forthcoming overtures are rebuffed, however, expect York to turn aggressive. First stop: Wall Street, where his glowing reputation as CFO at both Chrysler and IBM ensures that he will, at least, get a fair hearing.

But there's little chance York will find any support at Chrysler, where executives are girding for another nasty fight. "We have recognized since last April that Tracinda was not a friendly shareholder and they had their own agenda based on self-interest," says Denomme. And Lutz, for one, says: "I would ten times rather work for a Chrysler run by Bob Eaton than a Chrysler run by Jerry York." To head off Kerkorian, Eaton met last month with a half-dozen Chrysler investors. He plans to address the annual meeting of the Council of Institutional Investors Oct. 3 in New York.

While the battle may heat up fast, Kerkorian is in no hurry to get what he wants. "Before he makes a move he gives it a lot of thought," York says. And like his 78-year-old boss, York knows there are many moves yet to go. "Think of this as a chess game, and at some point you want checkmate," he says. "Checkmate is a material increase in market value." And for York, perhaps, something more: Eaton's job.

By Bill Vlasic in New York, with Keith Naughton and Kathleen Kervin in Detroit

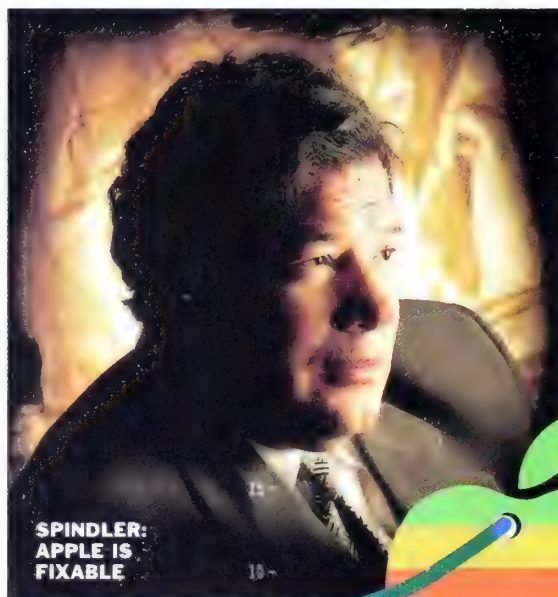
## STRATEGIES

### IS SPINDLER A SURVIVOR?

Despite lots more bad news, Apple's board says he's staying

**T**he hot gossip in Silicon Valley? Apple Computer Inc. Chief Executive Michael Spindler is in big trouble with his board. And if Apple's stock keeps sinking—it's down to \$37 from \$48 in mid-July—rumormongers say the company may be faced with an unwelcome bid from one of several interested suitors—including IBM and Oracle Systems.

Don't bet on either. Despite three



straight quarters of disappointing results, including the company's announcement on Sept. 14 that fourth-quarter earnings would be lower

than expected, Apple directors appear to be solidly backing their man. "The board has great confidence in Michael Spindler," says Bernard Goldstein, an Apple director and a partner at venture-capital firm Broadview Associates. "We think he's an extraordinary chief executive." And Spindler dismisses the takeover talk, saying Apple isn't a good strategic fit for any of the rumored suitors.

That's not to say Spindler isn't facing some serious problems. Demand for a new wave of Macintosh computers is booming—the company's backlog is

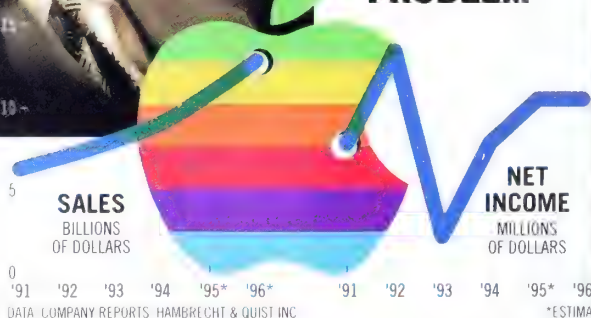
more than \$1 billion—but Apple can't cash in on the surge with stepped-up production because it lacks critical parts, including modems and custom chips. And since Apple won't be able to get extra supplies from parts makers already deluged with orders, the company won't be able to make the most of one of the hottest Christmas selling seasons ever.

To be sure, parts shortages are plaguing all PC players. But Apple's are the worst. That's because many of its components are custom-designed and sourced from one supplier. In practice means that accurate forecasting is critical. And there, insiders say, Apple goofed. The company underestimated demand for 1995, predicting growth of 15%. So far, sales have

surged along at 25%. The problem, say senior Apple executives, is that Apple's salespeople are "sandbagged" top executives by forecasting sales that they knew could easily be surpassed in order to enhance their own performances.

Spindler says Apple's difficulties are fixable. "I don't see this idea that we have systemic problems," he says. Still, Apple's profits will be flat in 1995. And it won't gain market share this year.

### APPLE'S PROBLEM

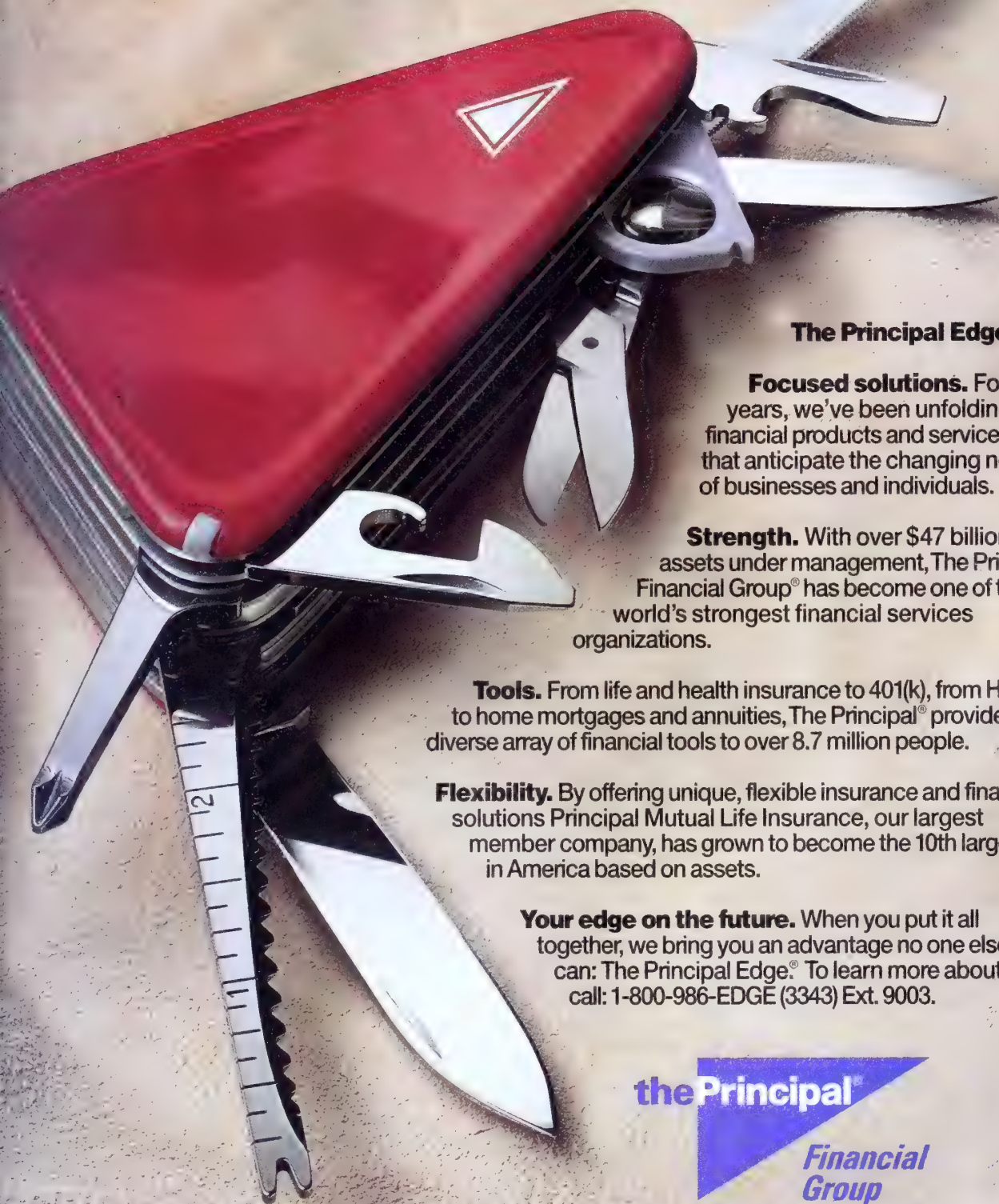


as Spindler had previously promised. Instead, since some consumers will be unable to find an Apple computer to buy, it's likely many will turn to computers running on Microsoft Corp.'s new Windows 95 operating system. That's leading some to begin nailing Apple's coffin shut. Says a former Apple senior executive: "There is no question Microsoft has won." Unless, that is, Spindler quiets down his critics by getting Apple back on track fast.

By Peter Burrows in Cupertino, Calif., with Kathy Rebello in San Francisco and bureau reports



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ENTERTAINMENT

# NEXT ON OPRAH: BURNED-OUT TALK-SHOW HOSTS?

Restless, Winfrey mulls a midlife career change

**M**any in the audience had arrived three hours before the 9 a.m. talk show began and were in a stomping, cheering frenzy when Oprah Winfrey strode onstage to begin her interview with Hollywood's Penny and Garry Marshall. She kept the show moving quickly and left many in the packed crowd atwitter at their brush with a talk TV icon.

Relaxing later, her feet up on a coffee table, Winfrey reflected on what an "inspiring diversion" the talk show was from her earlier ambition to become a film star. Still, she allowed as how the two-a-day, 200-a-year tapings of *The Oprah Winfrey Show* are now wearing her down. "I just don't have the time to do all of the other things I want."

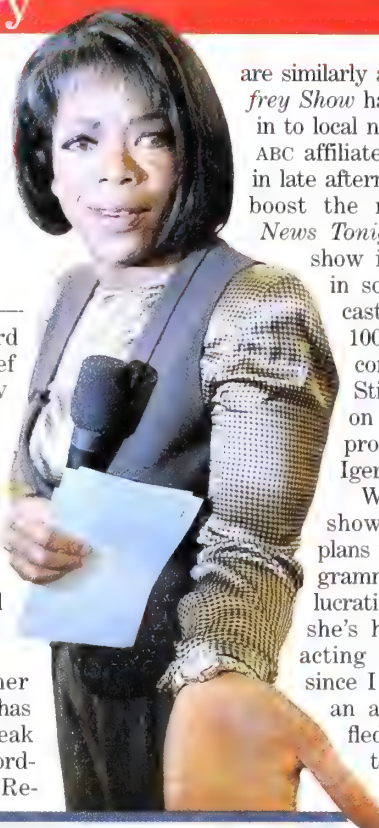
After 10 years atop the talk show heap, Oprah, at 41, is mulling a midlife career change. By Oct. 6, she must decide whether to exercise an option in her syndication contract that would make this the final year for the daytime show viewed by 15 million people in 119 countries. "I waver day-to-day," she says. The show is worth some \$75 million a year in revenues to her Harpo Entertainment Group. But Winfrey quickly adds: "This is not about money. I would like to feel I could have an impact on people's lives in a broader venue."

**MARRY A GIANT?** In fact, Oprah and her senior advisors are plotting a broad strategy to extend her wildly popular "brand name" across a wide range of media, playing to the growing appetite of emerging conglomerates for new products. The idea: to take Oprah Inc. into everything from movies and TV interview programs to fitness videos and on-line services, betting that her marquee name can translate into a series of hits.

Another possibility: linking Harpo's studio, fledgling film company, and library of more than 2,000 tapes with one of the new media giants—though no formal discussions have taken place. "Oprah is worth more and more...eve-

ry day," says Richard Frank, the former chief of Walt Disney Co.'s TV operations who recently joined Comcast Corp. to take its cable operations into programming.

Oprah may be picking just the right time should she bail out of daytime TV. Although still far and away the leader, her show's average rating has slipped to 8 from a peak of 10.5 in 1991-92, according to Nielsen Media Re-



## In the Boardroom With Oprah

*Future plans of Oprah Winfrey's Harpo Entertainment Group:*

**TELEVISION** By Oct. 6, Winfrey must decide whether to extend *The Oprah Winfrey Show* for an 11th year. She's interested in a prime-time network interview show and in May signed a six-picture, made-for-TV production deal with ABC.

**CABLE** Winfrey may use her 2,200 hours of shows as the core of a talk-show channel.

**VIDEOS** The born-again health nut is considering a line of fitness videos.

**FILMS** Winfrey has rights or options on nine books she wants to turn into films. She may act in some of them.

**ONLINE** *Oprah Online* debuts Oct. 2 on America Online in partnership with ABC.

DATA: BUSINESS WEEK

search. New talkfests such as Jenny Jones and Ricki Lake, plus competition from the O.J. Simpson trial and Oprah's decision a year ago to abandon the seamier side of chat—all have conspired to drive viewers away.

Winfrey insists the ratings slide will have nothing to do with any decision to drop the show. There's no question, though, that a lot of money rests on the outcome. The loss of Oprah would wipe out about 40% of syndicator King World Productions Inc.'s revenues. Winfrey holds 1.5 million of King World stock options, worth \$40 million, with the right to as many as one million more. That may lead her to develop another King World series.

Executives at Capital Cities/ABC Inc.

are similarly anxious. *The Oprah Winfrey Show* has long been a key let-in to local news shows for the many ABC affiliates that run the program in late afternoon. That, in turn, helps boost the network's ABC *World News Tonight* program. True, the show is pricey: Fees charged in some markets for broadcast rights rose by 20% to 100% under Winfrey's 1991 contract with King World. Still, "the absence of Oprah on a daily basis would be profound," says Robert Iger, president of Capital Cities.

Whether she extends the show or not, Winfrey plans to venture into new programming arenas, particularly lucrative prime-time ones. As she's hoping to pursue marketing opportunities. "Ever since I was 19, I wanted to be an actress," she says. Her fledgling film company is

the rights or options on nine books, including Toni Morrison's Pulitzer-winning *Beloved*. There's plenty of interest in Winfrey's far-flung plans. Before Turner Broadcasting System Inc.'s proposed purchase of King World collapsed, its executives mused with Harpo officials over what Scott Sassa, president of Turner Entertainment Group, describes as "a virtual Oprah"—a brand that could be pushed into everything from a woman's TV network to CD-ROM cookbooks. Winfrey already is building

on her relationship with ABC, with which she recently signed a deal to produce or star in six TV films. A prime time interview show on ABC also is possible. And on Oct. 2, the two will co-underwrite the debut of *Oprah Online* on America Online.

Away from the media bright lights, Oprah is "trying to stay grounded in reality." She's committing at least \$3 million to help 100 Chicago inner-city families leave their housing projects for new jobs and new homes. That's the sort of pursuit that increasingly gets her attention. The question: How much longer before she is distracted completely from daytime talk?

By Richard A. Melcher in Chicago with David Greising in Atlanta



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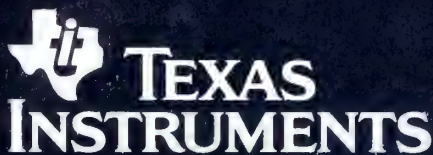
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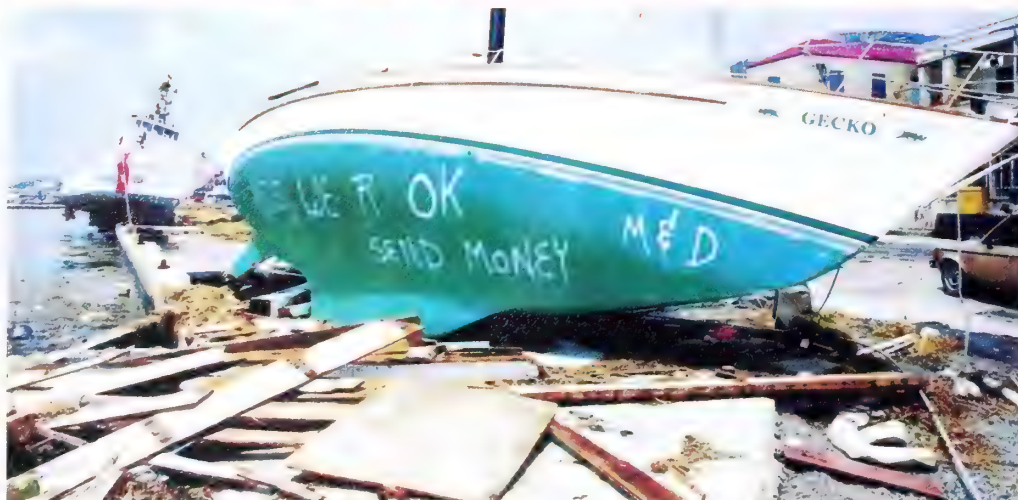
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**ST. THOMAS:** *Paradise lost, for now*

**TOURISM**

## WASTED AWAY: MARGARITAVILLE

Already, the Caribbean is suffering winter cancellations

**F**or the past eight winters, Ruth and Marvin Cohn have escaped the cold of New York for two weeks at the Pelican Bay Resort in St. Martin. But after Hurricane Luis lashed the Caribbean island earlier this month, the Cohns cancelled this season's trip. Now they're mulling a long weekend in New Orleans or a trip to the Carolinas. "I love St. Martin," says Ruth Cohn. "We will go back—but not this year."

Hardly comforting words for islanders, who are reeling from one of the worst hurricane seasons in memory. But as the region digs out from the trail of destruction left by Hurricane Luis, which pounded Antigua and St. Martin on Sept. 5, and Hurricane Marilyn, which pummeled the U.S. Virgin Islands on Sept. 16, much of the Caribbean is bracing for another hit—this one economic—as tourists seek sand, sea, and sun elsewhere.

**\$12 BILLION STAKE.** There's good reason for concern. While Marilyn devastated only St. Thomas, damaging at least 75% of its buildings, and dealt lesser blows to St. John, St. Croix, and some eastern islands near Puerto Rico, many travelers think of "the Caribbean" as a single

destination rather than as individual islands. So when there is bad news about one part of the region, says Jean S. Holder, secretary general of the Caribbean Tourism Organization, a regional tourism group, "inevitably, there is the potential it will have a negative impact on the entire region."

The worst-case scenario? That travelers will avoid the Caribbean altogether this winter. Last year, 14.1 million visitors and 3.3 million cruise passengers spent \$11.7 billion there. And the stakes for the individual island economies are staggering: Some 50% of the gross national product of Antigua and 60% of the gross domestic product of the U.S. Virgin Islands is derived from tourism. With damage from the storms likely to reach over \$1 billion, the region can ill afford to lose tourist dollars.

At this point, though, such a hit seems inevitable. "People are definitely shying away from the Caribbean because of the weather," says George Morris, a travel agent with Gables Travel in Coral Gables, Fla., who says he has seen a downturn in Caribbean bookings since mid-August. Where are people going? Myrtle Beach, S.C., reports an uptick in

bookings since August, and other sun seekers are heading toward friendly climates in California. Even if travelers wanted to get to the affected Caribbean island, they'd find the going tough. On Sept. 20, Continental Airlines Inc. announced it had suspended flights to Antigua, St. Martin, and St. Thomas.

**GOING WEST.** Still, the hurricanes might not hit the Caribbean economy as hard as some fear. That's because

many travelers are merely rebooking trips to islands not affected by the storms. Cruise line companies Carnival, Royal Caribbean, and Norwegian Cruise Line, for instance, are shifting passengers to other local ports of call. Carnival is diverting passengers to western Caribbean stops such as Cozumel and Grand Cayman. Royal Caribbean's *Monarch of the Seas* is calling on Trinidad, Barbados, and Martinique. And Norwegian Cruise Line substituted St. Croix after Luis damaged Antigua and St. Martin.

Indeed, as travelers assess their vacation plans, other destinations in the Caribbean—Aruba, Barbados, Curacao, the Cayman Islands, and Jamaica—could benefit, as will the coastal resorts of Mexico, travel agents say. Nadine Hodge had planned for a year to visit St. Martin with her mother and other relatives. Instead, they will travel to the Cayman Islands this fall.

Those islanders looking for reasons to be optimistic should consider the tip of the iceberg. The Siboney Beach Club in Antigua. It is already hosting adventurous European travelers who were curious about the aftermath of a hurricane. But unfortunately for the Caribbean, the attitude of Jennifer Castelli is likely to be far more common. The New Yorker spent part of her honeymoon in Antigua surviving the howling winds of Luis. Will she come back to the Caribbean? "Definitely not during hurricane season," she says. After this year's lesson, more travelers will no doubt say the same.

*By Gail DeGeorge, with David Swafford in Miami, and bureau reports*

The bad news: Tourists tend to think the hurricanes hit every island. The good news: Memories are short



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BASEBALL

# WHAT'S ALL THE BLUBBERING ABOUT? YOU'RE WINNING

The Red Sox could take the pennant but lose Fenway Park

*Fenway Park, in Boston, is a lyric little bandbox of a ballpark. Everything is painted green, and seems in curiously sharp focus, like the inside of an old-fashioned peeping-type Easter egg. It was built in 1912 and rebuilt in 1934, and offers, as do most Boston artifacts, a compromise between Man's Euclidian determinations and Nature's beguiling irregularities.*

—John Updike, *Hub Fans Bid Kid Adieu*, 1960

It is a fabled ballpark, home once to Babe Ruth, Ted Williams, Carl Yastrzemski, and now to Roger Clemens and Mo Vaughn (lesser deities, but deities still). Purists, even a few in the Bronx, insist that Fenway almost is baseball. But this national treasure soon will be no more.

Even as the Boston Red Sox chase their first league championship since 1918, the team's front office is trash-talking its stadium. Sox owner John Harrington says that tiny Fenway is "economically obsolete." Jealously eyeing gleaming new ballparks in Baltimore and Cleveland, he has launched plans to build a \$150 million, state-of-the-art replacement. The new park, says team Executive Vice-President John S. Buckley, "will have all the amenities."

Sox management has yet to hire an architect or traffic planners—or sort out

with city officials the nitty-gritty of the deal. But the team has said it will fund the cost of a new park if Boston provides the land. And both sides have tentatively agreed to a site in South Boston, just half a mile from the city's financial district. Buckley hopes a new park, with 50% more seats, will be ready in 2002, a year after the team's 100th anniversary.

Over some diehards' dead bodies, perhaps. Fenway "is the cathedral of baseball," says Boston native Thad Russell. Although he's now a Los Angeles adman, Russell plans to launch a "Save Fenway" campaign with billboards and print ads in Boston papers. Echoing the sentiments of thousands of Fenway faithful, he says: "We'll lose our best connection to baseball history."

From a fan's perspective, indeed, few big-league ballparks have Fenway's charm and quirks. With just 33,000 seats, nearly everyone gets a closeup view of the game. In left field looms the fabled "Green Monster," a 37-foot-high wall. In center, there's the "Bermuda Triangle," where fly balls can drop for a routine out, or, if hit a few feet to the left or right, wind up as home runs.

Buckley acknowledges that it will be hard to leave such eccentricities behind. But he says that if the Sox stay in Fenway, they will be at a serious competitive disadvantage. Baltimore's Camden Yards and Cleveland's Jacobs Field both have about 10,000 more seats than Fenway, plus lucrative plastic seats and luxury boxes (table). Revenues from Fenway, at \$70 million, are about 20% below those of both Cleveland and Baltimore, and "that money pays for a lot of salaries and a lot of developing players," says Buckley. Though the Sox boast one of the majors' most productive minor-league systems—and they are in first place. No matter: In today's big-money game, the Sox say they can't afford top talent without higher revenue.

**LUXURY BOXES.** Buckley says the team remains committed to a new ballpark that retains as much of Fenway's character as possible. The Green Monster would be moved in its entirety, along with Fenway's manual scoreboard, and pledged. The grass still would be reseeded. But the new park would have wider aisles and seats, updated bathrooms and numerous luxury boxes.

And the name? Well, it won't be Fenway. Like San Francisco, which is naming its stadium 3Com Park, thanks to a multimillion dollar contribution from

the computer networking company, that name, the Sox plan to auction off the right to name the new home. But of Boston Stadium Reebok Park? Green Monster or no, it just won't be the same.

By Geoffrey Sneed  
in Boston

## Bush League?

CAPACITY OF MAJOR LEAGUE BALLPARKS

|                           |        |
|---------------------------|--------|
| FENWAY PARK (BOSTON)      | 33,871 |
| JACOBS FIELD (CLEVELAND)  | 42,400 |
| CAMDEN YARDS (BALTIMORE)  | 48,079 |
| COORS FIELD (COLORADO)    | 50,000 |
| YANKEE STADIUM (NEW YORK) | 57,545 |

DATA: FODOR'S FOUR SPORTS STADIUM GUIDE







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EDITED BY KEITH H. HAMMONDS

## IF AT FIRST COLGATE DOESN'T SUCCEED...

CAN COLGATE-PALMOLIVE GET it right this time? The personal-care-products giant has restructured three times since 1984. On Sept. 20 came word of the fourth. Colgate announced a \$369 million makeover that will shutter or reconfigure 24 factories worldwide and reduce employment by 3,000, to 33,000. The company will take an earnings hit of \$2.54 per share for the third quarter and report a loss for the period—atop disappointing operating results. Colgate said savings from the reorganization would start to kick in during the second half of 1996 and with greater force in 1997. “The only disap-

pointment [about the restructuring] is that it will be a while before investors see any benefit,” says William Steele, a Dean Witter Reynolds analyst.

## IN DISK DRIVES, IT'S EAT OR BE EATEN

THIS DEAL COULD PORTEND A new round of consolidation in the bitterly competitive disk-drive business. On Sept. 20, Seagate Technology, the market's sales leader, announced plans to purchase No. 3 Conner Peripherals for \$1.1 billion in stock. The acquisition would create a \$7.6 billion company, more than double the size of No. 2 Quantum. And by buying Conner, which has struggled with manufacturing problems, Seagate would gain strength in the smaller drives used for personal computers.

## CLOSING BELL

### JUST DID IT

The athletic-shoe race is looking like a blowout. On Sept. 18, Nike announced fiscal first-quarter earnings of \$164.8 million, up 55% from the year before and far better than analysts had expected. Nike also served up a 100% stock dividend. The news was a slam dunk for investors, who pushed Nike shares up by 7%, to 99%—an increase of 40% since the beginning of the year. Rival Reebok International's shares, meanwhile, are down 10% for the same period. With footwear orders falling and ad expenses high, profits are slumping at Reebok, and key managers are bailing out.



## THE GLITCH THAT SHUT FORD'S PLANTS

FORD SHUT DOWN SIX PLANTS the week of Sept. 18 after at least one supplier couldn't deliver a key power-steering-systems component used in the Mustang, the Contour, the Crown Victoria, and in Ranger pickups. All together, the problem delayed production on a total of 20,600 vehicles. Ford says it can make up for the shutdown by ratcheting up production during the fourth quarter. That hardly seems necessary: Sluggish sales have bloated inventories on the affected models to 33% above normal.

## BIRTH OF A FORMAT FOR CDs?

WITH IBM LOOKING STERNLY over their shoulders, two feuding factions agreed on an important standard for the next-generation compact disk. It will use the optical

## HEADLINER: O.J. SIMPSON

### SQUEEZING DOUGH FROM 'JUICE'?

Outside the Los Angeles County Courthouse, vendors hawk “Free the Juice” T-shirts and photos of O.J. Simpson in his football glory days. Now, O.J. apparently has designs on that money.

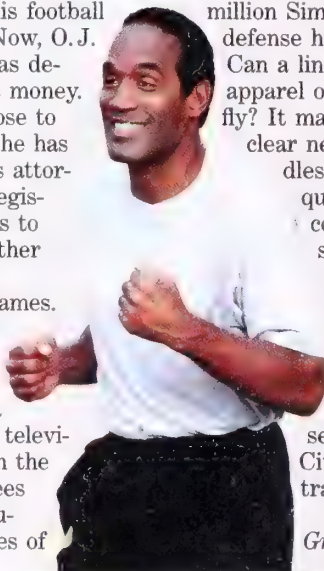
Sources close to Simpson say he has instructed his attorneys to file registration papers to trademark either his “O.J.” or “Juice” nicknames. This is in addition to his book, *I Want to Tell You*, a pay-per-view television special in the works, and fees from the thousands of pieces of

sports memorabilia he signs in jail.

All of it will go to help pay off the estimated \$6 million Simpson's legal defense has cost so far.

Can a line of “Juice” apparel or footwear fly? It may have to clear new legal hurdles first. “I'd question if he could copyright something that generic,” says Joseph J. Gleason, vice-president and general counsel of Florida Citrus Mutual, a trade group.

By Ronald Grover



format proposed by Toshiba and partner Time Warner and a recording scheme from Sony and Philips Electronics, ensuring that future players can handle today's audio CDs and computer CD-ROMs. Although promoted as the way to get consumers to buy movies on disk, the yet-unnamed product more likely will find its initial use in the fiercely competitive home computer business for multimedia game and “edutainment” software.

## THE NFL ROPES IN A MAVERICK COWBOY

YOU COULD SEE THIS LAWSUIT coming from a Texas mile away. All summer long, Dallas Cowboys owner Jerry Jones has been raising hackles within the National Football League's cozy inner circle by signing exclusive sponsorships with such non-NFL partners as Dr Pepper,

PepsiCo, and Nike. On Sept. 18, the league drew its line in the turf, slapping Jones with a federal suit seeking more than \$300 million in damages. The suit seeks a court order to bar Jones from striking any more renege deals, which the NFL says violates revenue-sharing rules. Jones insists the pacts violate nothing because they are with Texas Stadium, home of the Cowboys, not with the team itself.

## ET CETERA...

- Carl Icahn, like buddy Bennett LeBow, is seeking up to 15% of RJR Nabisco's shares.
- Stephan Weiss, husband of Donna, resigned as co-CEO of Donna Karan Co.
- MCI Communications will pay \$1 billion for SHL Systemhouse.
- The Senate Banking Committee agreed to combine bank and thrift charters by 1998.

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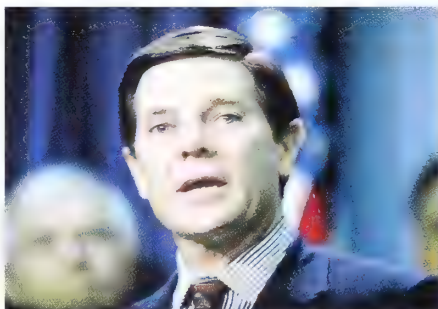
EDITED BY OWEN ULLMANN

## THE HOUSE ENFORCER ISN'T BLINKING

House Majority Whip Tom DeLay is a happy warrior. As chief vote-counter and head-knocker for the GOP revolution, the Texas Republican spends each day leading his troops in battle to claim what he calls "the fruits of our victory." Victory is simple to the 48-year-old former exterminator in suburban Houston: making sure that the GOP's ideological agenda isn't watered down by Capitol Hill moderates—even those in his own party. From free-enterprise economic policy to pro-family social issues, "I see myself as the line of offense," the No. 3 House Republican leader says. DeLay's uncompromising stance has emboldened the young House Republicans, who vow to go to the mat to enact their Contract With America. But such intransigence could spell trouble for House Speaker Newt Gingrich (R-Ga.). He must begin trade-ing with a less conservative President and a Democratic President if he wishes to salvage tax cuts, a balanced-budget plan, welfare overhaul, regulatory reform, and other key Contract planks. For now, the whip is pushing GOP leadership to stick with purity over pragmatism. As chief Contract enforcer, DeLay has the charge to slash government agencies, roll back environmental laws, restrict abortion, punish out-of-wedlock births, and promote public prayer. His red-meat rhetoric—he denounced the Environmental Protection Agency as "the Gestapo of government"—delights conservatives but makes moderates and liberals blanch. Snaps Gregory S. Wetzel, legislative director for the Natural Resources Defense Council: "He's about as extreme as anyone in this Congress." DeLay's firebrand rhetoric hasn't hindered his effectiveness: he has won 99% of all votes backed by the leadership. As for his own pet projects, "I haven't lost any," he boasts. He forced passage in a GOP telecom reform bill to make it more free-market. Now, he's blocking an antiterrorism measure which he

claims jeopardizes gun ownership rights and gives too much clout to the feds. Another current project: curb EPA and workplace-safety regulators. "I know a lot about pest control," he says, "and we're finding a lot of varmints up here."

That mix of hardline beliefs and hardball politics has been the hallmark of DeLay's public career. He ran for the Texas legislature in 1978 because he was unhappy with government regulation of his business, and his push to undo costly state rules on the trucking industry won him the nickname "Tommy DeReg." Despite his unyielding politics, DeLay's deft touch at building personal relationships since coming to Congress in 1985 helped win him the whip job.



NO "SQUISHY MODERATE": Whip DeLay

**FAST TRAIN.** But both DeLay's fervor and his friendships will soon be tested. Gingrich's conciliatory talk about finding common ground with Senate moderates and the White House on a budget plan to avoid a "train wreck" that would shut down government could clash with DeLay's vow to protect the GOP Contract.

The Texan denies the party leadership is split. "We can play good cop, bad cop," he insists. But it's a dicey strategy. A stubborn stand for purity could alienate moderates and sink leadership hopes for

even modest achievements, such as cutting student loans, easing environmental controls on business, or reforming welfare. Yet too much compromising may provoke an insurrection from the 73 House GOP freshmen who sometimes, jokes DeLay, make him feel like a "squishy moderate."

In the end, a conservative rebellion could sink legal reform, regulatory curbs, and family tax breaks. That would be fine with the hardliners, who'd then run on the issues in '96. But DeLay has counted heads and is betting that his thunder on the right will convince Gingrich that cutting too many deals with Hill centrists or Bill Clinton could be a dangerous game.

*By Richard S. Dunham*

## CAPITAL WRAPUP

### HELMS'S UNDIPLOMATIC MOVE

U.S. ambassadors from four Asian nations won't be in place to greet Bill Clinton at November's Asia-Pacific Economic summit in Japan. Envoys to China, Malaysia, Thailand, and Indonesia are among 30 nominations Senate Foreign Relations Committee chairman Jesse Helms (R-N.C.) is blocking. Why? It's payback for Clinton opposing Helms's bill to kill the Arms Control & Disarmament Agency, Agency for International Development, and U.S. Information Agency.

### TONING DOWN TRADE TENSIONS

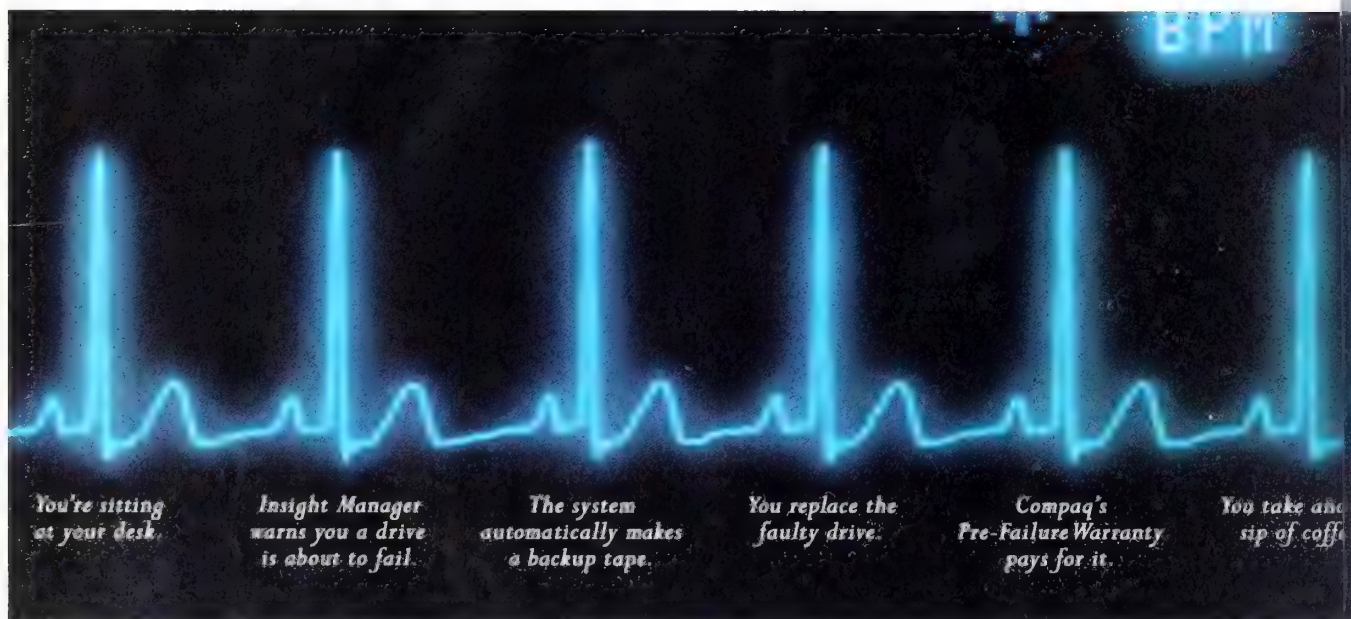
► Weary of trade battles with Japan over semiconductors, autos, and telecommunications, the U.S. wants to try conciliation. One idea: resurrect a U.S.-Japan committee to resolve trade skirmishes before they turn into full-blown wars. The panel was established by the Bush Administration, but the Clintonites let it die. Lee Sands, a top Japan hand in the U.S. Trade Representative's office, is expected to discuss reviving the panel when he travels to Tokyo this fall.

### OPERATION R&D RESCUE

► President Clinton will soon launch an offensive to shield his favorite science and technology efforts from GOP budget slashers on Capitol Hill. So far, Clinton has been silent about planned cuts for projects ranging from the Commerce Dept.'s Advanced Technology Program to global warming research. But on Oct. 18, he's set to make a detailed defense of government R&D. The pitch: These are crucial investments, not "corporate welfare," as Republicans charge.



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**T**hree million Italians poured into the country's auto showrooms during the Sept. 15 weekend to get their first look at Fiat's newest cars, the Bravo and Brava midsize models. "The turnout was incredible," says Andrea Colaneri, manager of Mondo Auto, a Rome dealer. "We're finally seeing a well-heeled crowd of yuppies and families again."

But now, the big challenge—in Italy and elsewhere in Europe—is to turn gawkers into buyers. As the car-buying season kicks off, with a record 20 new models hitting the market, industry executives are blanching at estimates that sales in Western Europe will increase by only 1% this year, to 12 million vehicles. Manufacturers had originally hoped for gains of up to 4%. "We are still suffering from the effects of the recession," says Graham Dymott, a spokesman at Britain's Society of Motor Manufacturers & Traders. "Business has recovered its confidence, but the private purchaser hasn't."

The carmakers will have to hone their marketing skills to turn these timid souls into customers. If they don't, the prospects are grim. Profits, recovering only slowly from the 1993 recession, could be hammered if the market doesn't pick up. The industry is already facing overcapacity of 2 million vehicles a year. Nervous executives at the recent Frankfurt Auto Show were wondering if a shakeout would force mergers upon Europe's smaller players.

**CROWDED TRACK.** It certainly doesn't help that so many new models are having to jockey for position in this anemic market. Renault's Mégane, a replacement for its R19, will be competing head-on with the Bravo and a new Rover 400 in the lower-priced midsize segment, which accounts for nearly one-third of European sales. General Motors Corp. is launching a new full-midsize Vectra model from its German Opel and British Vauxhall units. Adding to the stampede in the full-midsize category, France's

## EUROPE

# WHO'LL BUY THESE CARS?

Auto makers must find customers for a glut of new models

### PEUGEOT 406

\$22,399. Battling a weak home market



### GM OPEL VECTRA

\$20,912. GM's big hope in Europe

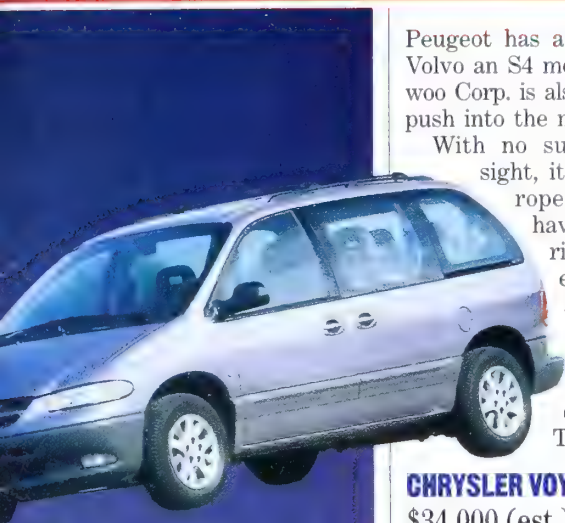


### FIAT BRAVA

\$24,000. Loaded with standard features







Peugeot has a new 406 and Sweden's Volvo an S4 model. South Korea's Dae-woo Corp. is also planning an aggressive push into the market.

With no sustained sales boom in sight, it's sinking in among Europe's carmakers that they have to imitate their U.S. rivals by wooing customers with new features and innovative pricing. "The days are past for manufacturers to believe they will be [just] order-takers," says Rod T. W. Ramsay, marketing director at Rover Group Ltd. Adds Karl E. Ludvigsen, chairman of London auto consultancy Ludvigsen Associates Ltd.: "It's a buyer's market now."

That means being acutely conscious of the tight constraints on buyers' budgets. Spending power is being drained by governments eager to slash huge budget deficits. France has already slapped two percentage points onto its value-added tax, raising it to a standard of 20.6% of the price of goods. French levies on gasoline are going up as well. Germans are paying a 7.5% surcharge on their tax bills, while the British Treasury is mopping up \$26 billion more in taxes from its citizens than it did two years ago.

**VOLVO S4**  
\$23,600. Roomy as a small Mercedes

The easy way to appeal to pinched buyers would be to cut prices. Not surprisingly, Europe's

carmakers want to avoid a sticker-price war if possible. Renault in particular wants to protect its margins, as the French government prepares to sell its 51% stake in the company in a weak stock market.

So marketers are trying to deliver value in other ways. A key strategy is to give a lot more car for the money.

Fiat's Bravo, for instance, will be offered in export markets with such goodies as a built-in stereo, central locking, a fire-



**FORD FIESTA**  
\$12,358. Looking to lead in the compact class



prevention system, driver's-side air bag, and electric windows as standard features—features once restricted to up-market models. And customers love it. More than price discounts, says Michel Kekus, salesman at a Peugeot dealership in Paris, "customers are looking for lots of options included in the price."

For drivers still worried about affordability, leasing is quickly gaining ground, much as it has in the U.S. Ingvar M. Sviggum, director of sales and marketing at Ford Werke, for example, says he is pushing leases extremely hard to try to get a leg up on competitors. This year, 30% of Ford Motor Co. vehicles in Germany were leased, up from just 10% last year. Ford advertising is focusing on the monthly payments, which are lower if you lease than if you buy.

**SHEEP AND GOATS.** European makers are also racing to deliver the hottest-selling products. That's a sea change from the past, when manufacturers measured the appeal of new models by the length of waiting lists. Says Mercedes-Benz CEO Helmut Werner: "Clients [nowadays] aren't willing to wait months for their cars." It's just as well the Europeans have heard the wake-up call. Honda Motor Co. CEO Nabuhiko Kawamoto bragged in Frankfurt that he's aiming to slash delivery time from factory to dealer from one month to one week for models such as the newly made-over Honda Civic.

Adding to the pressure in this crowded market is that quality and performance don't separate the sheep from the goats in the way they used to. In those respects, says Peter Davis, Fiat's director of design in Turin, "all the [new] cars are great cars."

To differentiate itself, Fiat is betting on Italian design and styling flair. Others figure that superior service in the showroom and after the sale could be winners. GM has already put more than 10,000 of its European employees and dealers through a program modeled on its Saturn unit's successful training scheme in America, which stresses low-pressure selling tactics.

Whatever strategies the carmakers adopt, a robust European market of 15 million units a year, once assumed to be just around the corner, now looks farther off than ever. But there could be a silver lining: Companies that survive profitably in the tough European markets have a good chance of emerging as the global competitors they aspire to be.

*By John Templeman, with David Woodruff, in Frankfurt, Silvia Sansoni in Rome, and bureau reports*



## SOUTH KOREA

# SEOUL FINALLY DIALS COMPETITION'S NUMBER

A two-step plan to open the \$8 billion telecom market

Car salesman Lee Ki-Hoon spends long hours commuting to different companies to sell fleets of vehicles. He thought a cellular phone would allow him to stay constantly in touch despite Seoul's monstrous traffic jams. But the top-of-the-line \$1,200 Motorola cell phone he bought is now locked away in his office drawer because of poor service from Korea Mobile Telecom. "After six months, I gave up," laments Lee. "You can hardly get connected. If you do, there's a good chance you won't be able to complete the call."

Help, though, may be on the way, partly thanks to U.S. government complaints about Korea's closed market. To appease Washington but also to make Korea's industry stronger, Seoul has unveiled a two-step plan to open the country's \$8 billion telecom market. Initially, the government will allow domestic companies to compete in all major telecommunications service areas except local calls and low-orbiting satellite communications by the end of 1996 (table). That will help them gear up for the second stage, when the government says it will let in foreign competitors around the end of 1997.

**GLOBAL EXPLOSION.** As a result of the gradual opening up, service already is starting to improve. Korea Mobile Telecom, which hasn't coped well with a nearly tenfold increase in subscribers, to 960,000 in the past five years, in August placed an order for \$100 million worth of equipment from AT&T to improve its switching and connecting. The company, which was taken over by Sunkyong Ltd. from the government in 1993, faces new competition from Shinsegi Mo-

bile Telecom. That rival, a consortium led by Korea's steel giant Pohang Iron & Steel Co. (POSCO), will begin providing cellular service in April, 1996, using technology developed by Qualcomm Inc., of San Diego.

The reason the government is stepping up the pace of liberalization is its fear that Korea might not be able to take advantage of the global explosion in information and computer technology fast enough. Experts say Korea should

be providing video-on-demand and home shopping through online services at a competitive price to most of its population. But access to international service such as CompuServe, still must be routed through a domestic provider, which costs a subscriber 30¢ a minute at a speed of only 2,400 bits per second, whereas 14,400 is standard elsewhere.

The deregulation plans also call for reshaping state-owned Korea Telecom into a long-distance operator as well as the sole provider of local services. As a first step, the government will expedite the carrier's privatization and grant it full managerial autonomy. Once privatized, the company, with \$6.8 billion in annual revenues, will be freed from regulatory shackles.

Korea Telecom does have one homegrown competitor, privately held DACOM. It already offers international calls and plans to begin domestic long distance in 1996. This step-by-step process of introducing second players to challenge state-owned monopolies leads most foreign experts to believe the government plan to take further steps is serious. "They've had a very pragmatic and structured approach in introducing this kind of managed competition," says Ken Zita, telecom consultant with Network Dynamics Associates Inc. in New York. "That's something other governments in the region are looking at."

One of the most controversial questions when it comes to telecom liberalization is what role Korea's big conglomerates, or *chaebol*, should play. Because concerns that the groups are too powerful, there are entry barriers and restrictions on ownership of even the privatized provider. The Samsung and LG groups, for example, can each own no more than 10% shares of DACOM, because they also manufacture equipment.

But as the government gears up for the next round of opening, there are at least 10 conglomerates, including Samsung, LG, Hyundai, and Daewoo, as well as steel giant POSCO, scrambling for a piece of the action. Korea ex-



## KOREA'S TIMETABLE FOR PHONE DEREGULATION

**CELLULAR PHONE SERVICE:** Complete deregulation this year

**INTERNATIONAL LONG-DISTANCE CALLS:** One new provider will be selected in 1996

**PCS SERVICE:** Five new providers to be selected by 1996

**WIRELESS DATA SERVICE:** Three new providers named by 1996

**DOMESTIC LONG-DISTANCE CALLS:** One new provider to be selected by 1996

**SATELLITE COMMUNICATIONS:** Details to be announced in 1996

**LOCAL PHONE SERVICE:** One new provider to be selected by 1997

DATA BUSINESS WEEK

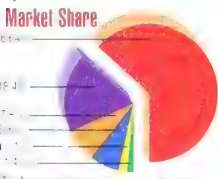


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pects to invest \$50 billion over 15 years, which will be difficult without bigger *chaebol* participation.

There also will be a role for foreigners, even while they are still barred from offering phone service. That's because the Koreans need capital and a wide range of technologies that only foreigners have, says Park Jong-Hyun, an analyst for LG Securities in Seoul. So big U.S. and Eu-

ropean players may be able to form more joint ventures in online services and cellular and personal communications services. For example, three U.S. companies—Air Touch, Southwestern Bell, and Qualcomm—already have a combined 20% stake in Shinsegei Mobile.

Making early inroads may prove critical. By the end of 1997, the Koreans hope that some of their telecom service

providers will be tough enough to compete against AT&T, BellSouth, or Cable Wireless of Britain in such countries as India, Vietnam, and China. That means they also will be more potent competitors at home. So even though the Koreans are gradually opening to outsiders, they clearly want to keep most of the important gains within the family.

*By Laxmi Nakarmi in Seoul*

## FOLLOW-UP

# READERS TAKE A SHINE TO HONG KONG'S APPLE DAILY

Jimmy Lai's hard-hitting new paper is flying off the newsstands

**H**ong Kong entrepreneur Jimmy Lai knew he was asking for trouble by starting a newspaper this summer. Lai had already angered Beijing after publishing an article blasting Chinese Premier Li Peng in *Next* magazine, Lai's top-selling weekly (BW—Dec. 5, 1994). Wary of offending China, investors developed cold feet and banks declined to lend him startup funds. Lai committed \$100 million of his own fortune to put his new *Apple Daily* on the streets.

Despite the long odds, *Apple Daily* is looking like a success just three months after its launch. According to Lai, the 290,000 issues printed each day sell out. To keep up with demand, Lai's printers are purchasing another press that will allow him to add another 100,000 issues a day by next April. Lai expects the paper to break even in November, when it rakes in \$168,000 a day in advertising revenue. Of the \$100 million Lai earmarked for the paper, he has spent about \$32 million. Lai predicts that annual revenues from his media group, which consists of four publications, will surpass those of Giordano Holdings Ltd., the \$370 million retail chain he founded, in just four years. Lai is selling his 37% stake in Giordano to concentrate on his media business.

It remains to be seen whether *Apple Daily* will be able to challenge market leader *Oriental Daily News*.

There are 60 Chinese-language newspapers in a territory comprising 6 million residents. Hong Kong's Audit Bureau of Circulations doesn't yet have figures to release for *Apple Daily*, but Anthony Lau, ABC's chairman, says that "early indications are that it is firmly established in the market—and that's quite a miracle."

Lai's reputation as a proponent of

freedom of expression certainly wins him points with some readers. Lai publishes exposés on everyone from criminal gangs to the wealthiest tycoon. And unlike most newspapers, which have shunned consumer news, *Apple Daily* runs six pages of it. Sensational stories have also run, but after a gruesome picture of a dead child created public outcry, Lai now promises to be "very sensitive about children who are victimized."

**MOB THREATS.** Unlike *Next* magazine, *Apple Daily* has yet to take on China—and Lai is not going out of his way to stir up trouble with Beijing. "If nothing is happening, why irritate them?" he says. Still, on any given day Lai has an average of 24 reporters in China, traveling on tourist visas since

Beijing won't provide the with journalist credentials. Recently two *Next* reporters were arrested in Fujian province. To Lai's relief, China released them in a few days. "I tell them, 'If you guys get caught, I can't help you,'" Lai says. "But they like the risk."

*Apple Daily* offers its 80 employees other rewards as well. It pays reporters 30% more than the competition, and senior staffers get stock options. That's a good incentive given the headaches they face. Mobsters have been making threatening noises, and some corrupt business executives have tried to bribe news editor Lai remains undaunted about that—and about Beijing's takeover of Hong Kong in 1997. "I don't think the Chinese are going to come here and break us down, because they need stability," he says. Lai's goal is to make his paper as strong as possible as he braces for the rough ride ahead.

*By Joyce Barnathan in Hong Kong*



**CHINA WATCHER:** Lai's *Apple Daily* hasn't yet angered Beijing



Shannon Anderson telecommutes from Everett, Washington.  
Which she finds easier than spending a minute longer in the office than she has to.

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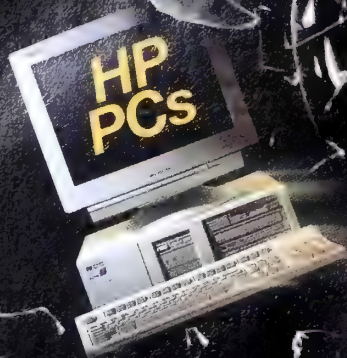
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EDITED BY STANLEY REED

# HONG KONG: 'WE ARE MOVING INTO MAJOR CONFRONTATION'

Just a few weeks ago, Britain and China seemed well on the way to a relatively painless handover of Hong Kong in 1997. The two sides had finally signed off on funding for the territory's new \$20 billion airport and seemed likely to work out other contentious issues. But with the surprisingly narrow victory of Martin C. M. Lee's crusading Democratic Party in the Sept. 18 elections for Hong Kong's Legislative Council (LegCo), all bets are off. "We are moving into a major confrontation," says John Walden, a former senior Hong Kong official. Most of the tension is likely to rise between the people of Hong Kong and China rather than between Beijing and British Governor Chris Patten. The election results revealed that China's efforts to win the support of Hong Kong's residents by buying into local companies and cultivating key figures have failed. **ACTION.** The vote was a clear slap in the face for Beijing. The three leading pro-China candidates lost, while the opposition, whom Beijing dismisses as a "counterrevolutionary," romped to a landslide victory. This shows China's multiparty "politics are here to stay," says Paul M. F. Cheng, a prominent legislator.

Although Beijing still says it will dissolve LegCo when the takeover happens, Chinese representatives in Hong Kong publicly backed candidates, and China parties mounted a big advertising campaign urging voters to support people who could get along with Beijing. Voters resoundingly rejected this message, favoring pro-democracy candidates in 17 of the 20 seats open to direct election. Lee and his allies came close to an overall majority in the 60-seat legislature, most of which is elected by voters representing specific occupational constituencies. "China made the polls a referendum on its involvement in Hong Kong," says Lee. "Now, China knows the answer." Over the next year and a half, the uncompromising Lee is likely to use his strength in LegCo to reopen sensitive issues,

such as the Court of Final Appeal, that were previously settled. Clearly, British flexibility will be reduced, and business worries that the Democrats will also obstruct contracts and push to cut the flow of immigrant labor.

Lee's strategy appears to be to carve out as much of a separate identity as he can for Hong Kong before the handover and then hope pressure from countries such as the U.S. and the international business community will provide some protection. This could work, but the danger is that the activist U.S. Congress could turn Hong Kong into another U.S.-China flash point like Taiwan.



**LANDSLIDE:** Lee, third from left, toasts his win

Much depends on whether the international and Hong Kong business communities can prevail on China to live up to its promise to give Hong Kong a "high degree of autonomy" in running its affairs. Hong Kong's Trade Development Council, the powerful government-funded business body, is already working hard to persuade mainland officials that Hong Kong will be more valuable to China as a semiautonomous entity than as just another Chinese city.

But on the whole, Lee's win has made already jittery business executives even more nervous. They worry that Lee, a British-educated barrister, will so annoy Beijing that Hong Kong's role as a business center will be wrecked. "If Hong Kong is perceived as a threat to China, then they won't listen to anybody," warns a leading Hong Kong businessman, who terms Lee's victory "bad news."

That isn't entirely fair. If Lee succeeds in his efforts to assure Hong Kong an accountable government and a fair legal system, the territory's position as Asia's most dynamic commercial center will be enhanced. The question is whether he can protect Hong Kong without provoking the Chinese into destroying it.

*By Mark L. Clifford, with Pete Engardio, in Hong Kong*

## GLOBAL WRAPUP

### MEXICAN SOCIAL SECURITY

Mexico plans to give Congress proposals soon for a major reform of its social security system. The plan, says Finance Secretary Guillermo Ortiz, is to switch from the "pay as you go" system to individual, capitalized accounts. Ortiz says the government will eventually have to fund the new system at the tune of 1% of domestic output each year for the next 5 to 6 years. But he hopes the change will eventually

raise the low domestic savings rates that figured in the peso crisis.

Ortiz is optimistic about efforts to bring international companies into Mexico's long-closed natural-gas sector. He said such companies could soon be building gas-distribution systems in Monterrey and elsewhere in northern Mexico.

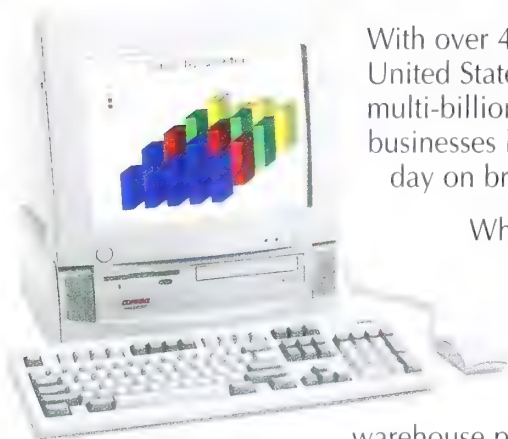
### EXIT IN SHANGHAI

► The general manager of the Shanghai Stock Exchange, Wei Wenyuan,

has stepped down under pressure from Beijing. Wei presided over rapid expansion of the exchange to its current \$30 billion capitalization, but fast growth also contributed to a rash of scandals that gave Beijing an opening to push him out. His replacement, Yang Xianghai, will likely be more conservative. He will put more emphasis on regulation, while slowing new issues and braking controversial plans such as opening the A-share market to foreign money.



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## Special Report

# ENTERPRISE

## Timely Insights for Small Business

### in Box page 2

os on health care, advertising, and other issues  
trepreneurs may find especially thorny

### Business Outlook page 4

ere there's a shortage of skilled workers,  
w are small businesses to compete with deep-  
pocketed megacompanies?



### Management page 6

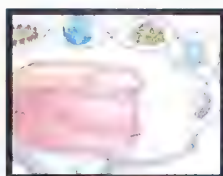
Train, train, train: From vendors to  
community colleges, how to foster  
the worker skills that make those  
fancy new machines worth the cost

### Companies page 10

th Magic: The Gathering, a fantasy card game,  
zards of the Coast has toppled mighty Dungeons  
Dragons as No. 1. Can it keep the sorcery going?

### Marketing page 13

e San Francisco quake of  
literally buried Laurence  
trow's pants business.  
w he's using the Net to dig  
nself out from under



### Technology page 16

Building a network is likely to  
be a grueling task for small  
business. But oh, the rewards

### International page 22

Capital is a rare enough commodity for any startup,  
but in Japan it's particularly hard to come by

### Roundtable page 28

Mr. Patricof goes to Washington, on small business'  
behalf—and finds the town  
surprisingly receptive

### Finance page 29

Equal (funding) rights for  
female entrepreneurs: New  
venues are easing the way



### At Your Service page 36

Dial "D" for deal: A call to a telephone reseller  
could cut your long-distance bill by as much as 35%

### Wit's End page 39

Connoisseurs of arcane, annoying rules and regs are  
certain to savor the government's definition of grits



# INBOX

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## Advertising on Two Fronts



To make the most of your advertising dollars, use a "two-pronged attack," says Rao Unnava, associate professor of marketing at Ohio State University's Fisher College of Business. His research shows it's best to run a few ads in the same medium as your competition, while also advertising in a medium your competition ignores.

In a controlled setting, Unnava measured students' recall a day after they had read and heard a series of

ads. He found the effectiveness of advertising drops substantially when there is "competitive interference." But if the advertising is in a different medium than the competition, its effectiveness is preserved. He suggests undermining your competitors ads in their chosen medium, while also seeking out virgin soil for your ads.

His research, published in the *Journal of Marketing Research*, found using one radio and one print ad was much more effective than two print or two radio ads. It was also more effective than launching a media blitz.

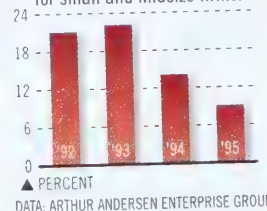
## FAMILY-BUSINESS SCHOOL

Learn how your family-owned business is affected by race, culture, and ethnicity; bone up on online commerce; and gain insight into how family relationships and business interact. These and other topics will be addressed at the Family Firm Institute Confer-

ence, in St. Louis on Oct. 11-14. Along with business owners, various professionals, including financial advisors, lawyers, accountants, and insurance agents, who specialize in family business will attend. Call 617 738-1591 for more information.

## Slower Climb For Health-Care Costs

Average increase in insurance fees for small and midsize firms:



## HEALTH COSTS: DON'T RELAX YET

Business owners aren't fretting about health-care costs the way they were last year. A recent survey conducted by Arthur Andersen's Enterprise Group found that 24% of small and midsize business owners, down from 42% in 1994, listed providing health benefits as among the most significant challenges to their future.

One reason concern is down: Premium costs aren't rising as rapidly. But don't be too complacent. Now that the pressure is off health-care reform, "you might start to see providers of care increase costs more to make up for what they see as lost ground," says Ruth J. Lee, a health-care consultant for Arthur Andersen in Chicago.

## Gender Watch

Women entrepreneurs: If you thought years of getting less than men for doing the same job were over once you started your own business, guess again. A recent on the earnings of self-employed women found they earned less than self-employed men. In the pay gap between men and women are self-employed even larger than

### FREE STUFF

- Learn how to prepare for disaster with *Insuring Your Business Against a Catastrophe*, the Insurance Information Institute (800 433-0307) for a copy of the nine-page brochure.
- Seeking financing for the time? The Federal Reserve of New York has published a guide that's useful for entrepreneurs in any state. To request a copy of *The Credit Process Guide for Small Businesses*, call 212 720-6134.



## B-schools and Small Biz: A Partnership at Risk

It seems like such a good idea: Team up business schools with local small companies in need of advice and have students, supervised by professors, provide free consulting. But a program that has successfully done just that for 23 years may fall under the budget axe this year.

The Small Business Administration hasn't requested funding from Congress for the Small Business Institute program this year. SBI doesn't reach as many people as some less expensive SBA programs, says Monika Edwards Harrison, an administrator at the SBA.

But all is not lost. In the past, Congress has restored SBI funding—and it still may. Plus, some universities plan to continue the program without the SBA's assistance, if necessary.

teen male and employees

employment is y of escaping ation," says a. Starr, senior t at the Office mic Research small Business

Administration, which funded the study. Its title: *Business Ownership as an Employment Opportunity for Women*, by Steven Lustgarten.

The study also found that the more client contact required, (as in sales), the greater the earnings differential between men and women. "It highlights a source of discrimination that doesn't usually show up," says Starr.

### WIDER EARNINGS GAP FOR SELF-EMPLOYED WOMEN Average earnings for women and men in 1990

| EMPLOYED | EMPLOYEES |
|----------|-----------|
| men      | Women     |
| \$6,652  | \$20,152  |
| en       | Men       |
| \$9,937  | \$31,123  |

DATA: SMALL BUSINESS ADMINISTRATION

## Help for the Home-based

Professional organizations are springing up to support home-based businesses. Independent Business Alliance (800 450-...) can hook you up with health and life insurance, financing, marketing help, and name-your-business product for \$24 a year, to become



"the AARP of this market segment," says Chairman Robert J. Levine.

SOHO America (800 495-SOHO) doesn't offer insurance yet but comes with an Internet site, a business advice line, a computer support service, and a fax-on-demand library. Its goal, for \$48 a year, is to serve small businesses as their "silent partner."

## KEEPING UP

As the number of employees grows, so do the regulations to comply with

- 1 EMPLOYEE ▶ Check work eligibility
- ▶ Pay overtime
- 11 ▶ Adhere to Occupational Safety & Health Administration (OSHA) rules (service firms are exempt)
- 15 ▶ Meet requirements of the Americans with Disabilities Act
- 20 ▶ Comply with COBRA
- 50 ▶ Offer leaves of absence as required by the Family Medical Leave Act
- 100 ▶ Complete affirmative action plan (required for government contracts)
- ▶ File Equal Employment Opportunity reports
- ▶ File forms and distribute information to employees on pension plan, assuming you have one (per ERISA)
- ▶ File Employee Commute Option Plan

DATA: PEOPLE MANAGEMENT INC.

## MCI TARGETS WOMEN BUSINESS OWNERS

Phone companies often market to small businesses through professional groups. But MCI Communications Corp. may be the first to craft a program for women. Its Business Women's Connection program, available through a growing list of women's associations, offers discounted MCI services and publications to help women network. For information, call 800 48WOMEN.

## FOR YOUR LIBRARY

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# SMALL ISN'T BEAUTIFUL WHEN SKILLS ARE SCARCE

By James C. Cooper and Kathleen Madigan

**P**atrick J. Moquin has been on the job only since Aug. 1, and he's already reading the help-wanted ads. But that's part of his job as the first-ever vice-president of human resources for Unitrode Corp., a manufacturer of integrated circuits in Merrimack, N.H. Moquin is checking out the competition to see what Unitrode must offer to attract the design engineers and other professionals so crucial to the company's growth. "The price of admission is making sure you are paying a very competitive compensation package," he says.

**31% of small businesses expect to add employees in 1995, up from 16% in 1992**

Moquin isn't the only one on a quest for top-notch employees. With the U.S.'s healthy economy and tight labor markets, small companies across the nation will face the difficult task of filling jobs that require more than basic skills. From software developers in Seattle to machinists in Chicago, specialized positions are going unfilled, even as unskilled labor remains plentiful.

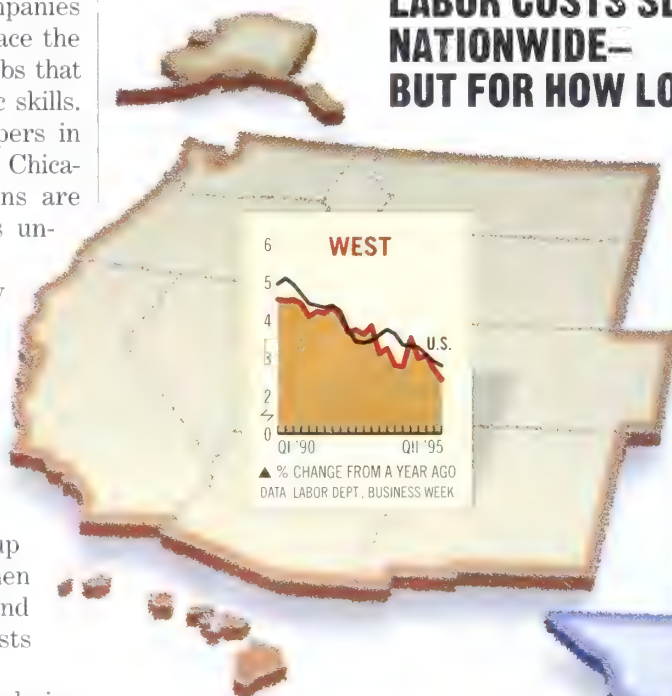
Small and midsize companies are increasingly worried about labor shortages and the near-certainty of having to sweeten the pot to attract skilled workers. Some 25% of companies with fewer than 500 employees cite a lack of qualified workers among their three most significant challenges, according to a joint study by Arthur Andersen & Co.'s Enterprise Group and National Small Business United. That's up from 20% in 1994 and 13% in 1993. In fact, when asked to list the top three hurdles to growth and survival, small businesses mentioned labor costs more often than even government regulation.

So far, the national trends in costs for wages, salaries, and benefits have glossed over these concerns. The growth in labor costs continued to slow in the second quarter—a pattern that held true in all major regions

(charts). However, the slowdown in labor costs is due solely to sharp cutbacks in what companies, mainly large corporations, are paying for benefits, which make up about a fourth of total compensation costs nationally. Because of slower growth in the costs of health care, workers' compensation, and state unemployment insurance, benefits grew only 2.6% during the past year, the slowest pace on record.

The downtrend won't last. The economic expansion already 4½ years old, has helped to push the national jobless rate down to 5.6% in August—below the level that is thought to be "full employment." Only 2.8% of the workforce is without jobs in the Research Triangle area of Raleigh-Durham-Chapel Hill, N.C. Even in Michigan—a state long associated with winding unemployment lines—the rate is just 5.1%. Moreover, the

**LABOR COSTS SLOW NATIONWIDE— BUT FOR HOW LONG?**



Regional employment costs for wages and benefits

omy is unlikely to de-  
erate enough to open  
much slack in the la-  
markets. The result:  
her costs to attract,  
in, and retain good  
employees.

The pressure can al-  
dy be seen in wage  
salaries, which make  
about 75% of labor  
ts nationally. Hourly

for the U.S. nonfarm sector is up 3% in the year  
ed in June, up from 2.5% a year earlier. At Walker,  
her, & Quinn Inc. (WRQ), a Seattle-based producer of  
nectivity software with a payroll of 150 workers,  
petition for technical talent has caused wage creep.  
ople are expecting a 10% salary increase if they  
nge jobs, and other companies are offering hefty  
ing bonuses," says Norris Palmanter, employment  
ector of the two-year-old company. WRQ has lost  
potential candidate because it could not match  
competition's bonus.

ndeed, most small companies have neither the cash  
the cachet of big-name corporations. To remain in  
hiring game, smaller companies must be creative in  
g their limited resources to attract the best job can-  
ates. It boils down to what the company can af-  
l. Cobra Electronics Corp., a  
cago-based maker of radar-  
ection devices that employs

## 23% of small businesses cite "lack of qualified workers" as the greatest obstacle next year

about 150 people, emphasizes perks such as flex-time, and it's using recruiters for the first time. Others simply bite the bullet and offer everything from child-care services to stock options to attract employees for key positions.

For most companies, though, the goal is to add workers without adding costs. One method: emphasizing flexibility and growth opportunities. "A lot of people are looking for the same technical people we are," says WRQ's Palmanter. "We let people have the freedom to be creative." At Seattle's Caffe Appassionato Co., a three-year-old retail and wholesale coffee company, a "barista" who makes espresso now may eventually become the store manager, says vice-president Tucker McHugh, who emphasizes promotion from within.

In today's information economy, the hottest market is

for workers with computer skills. Tivoli Systems Inc., a software maker in Austin, expects to add more than 100 new workers this year to the 200 already there. It's recruiting people with technical backgrounds, including

computer science and engineering, with salaries up to the low six figures for certain positions, says William G. Bock, senior vice-president for operations. One solution for Tivoli, which expects sales of \$40 million-plus this year, is subcontracting. It signed up 10 outside companies when its professional-services business, which offers computer consulting and training to customers, was overwhelmed by demand. Bock admits that using

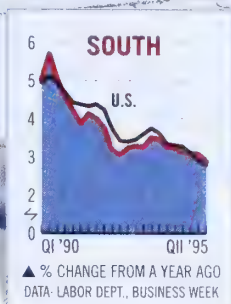
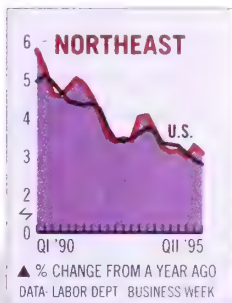
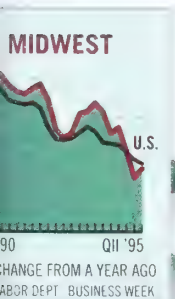
outsiders is more expensive, but the strategy gives

Tivoli quick access to a large pool of labor.

Of course, rising wages don't have to rob a company's bottom line. As long as new workers boost productivity, the addition to revenues covers the extra costs. At circuit maker Unitrode, the rule of thumb is to ensure that base-wage costs don't grow by more than half the pace of revenue gains. Still, there is no set formula for a fair and cost-efficient compensation package. "It becomes a matter of risk management," says Unitrode's Moquin. "How much are you willing to pay before you bastardize the integrity of the process?"

Don't expect the job scramble to level off soon. In a recent survey of small-business owners by KeyCorp, a bank holding company based in Cleveland, 38% expected their companies to grow in the coming year, up from 26% a year ago. That means demand for skilled labor will continue to outpace supply, positioning 1996 not just as a year of help wanted, but of help wanted desperately.

Compiled with bureau reports





# EXPLOITING THE PROMISE OF COMPUTERS

For small business especially, there's no technology payoff without the proper training





s the Industrial Era gives way to the Information Age, computers are changing the way we work and produce. Nowhere is technology's transformative power greater than among America's small businesses. Coming power that once cost hundreds of thousands of dollars can now be bought for a few thousand dollars in small and midsize businesses. Electronic messages, databases, networks, and other information technologies are animating the economy-of-scale advances enjoyed by Big Business for much of the post-World War II era. Savvy entrepreneurs are using high-tech equipment to reach new customers and exploit market niches.

One trouble is, while the technology pays for itself, many smaller businesses are covering the returns tough to come by. Far too often, a business will go out for razzle-dazzle hardware and software but neglect to invest in training workers to use their new tools productively. Experiences vary, of course. Nancy Corbett, director of benchmarking services at Coopers & Lybrand, says companies typically spend less than 5% of their technology budget on training. The optimal outlay: between 5% and 7%. "If you don't allocate the dollars to plan for training, the investment won't pay off," she says. Warns Terry L. Andersen, worldwide managing partner of Andersen Consulting's change management practice: "Think about training before you purchase any technology."

**GEPODGE.** Take the experience of Instron Corp., a Canton (Mass.) maker of materials-testing equipment. The \$136 million company spent millions of dollars on computers in the late 1980s and early 1990s. Yet some bookkeeping still relies around a ledger book that's been in use for 25 years. Every day, the serial numbers of components used by one of the company's units are entered by hand. A lot of other pencil-pushing goes on at Instron, too. When it started computerizing, the company bought a hodgepodge of software systems. Worse, few of the 425 employees at the company's facility were trained to use the new tools, even though personal computers were on most desks. "This was a classroom, where the company invested in technology and then just said, 'Here, go at it, guys,'" says Mark C. Montemayor, manager of manufacturing systems. About two years ago, senior executives said "enough." Now, they are installing a new corporate information system with standardized hardware and software platforms built around a network of IBM RS 6000 and Novell Inc. workstations. Instron contracted with outside trainer, Catapult Inc., a national company with offices in Boston, to

provide software training for employees, and budgeted between \$40,000 and \$50,000 from August, 1995 through August, 1996. The Massachusetts Manufacturing Partnership, part of a network of technical support programs sponsored by the National Institute of Standards & Technology, is providing \$12,000 in funding to subsidize the training. Says Montlock: "Without the training, we're just not going to be very productive."

That's a lesson more and more companies are taking to heart. True, a 1993 Bureau of Labor Statistics study found that only 52% of businesses with fewer

than 50 workers provide training to upgrade employee skills because of technological change, vs. 78% of businesses with 250 or more employees (chart, page 8). But smaller companies aren't neglecting employee training as much as the data suggest. It's just that many are far more likely to rely on on-the-job training and informal instruction. And, facing a shortage of skilled labor, 67% of small and midsize business owners say they now plan on investing in training programs, according to a survey by Arthur Andersen's Enterprise Group and National Small Business United.

The explosive growth of computers

## A Road Map To High-Tech Training

### SOURCE

#### National training

#### Local training or trade schools

#### Community colleges

#### Trade or professional organization

#### Local organizations, like the Chamber of Commerce

#### Unions

#### Mentors or coaches

#### Multimedia

#### Vendors and suppliers

#### Government-sponsored economic development centers

### ADVANTAGES

Trainers have broad experience with a wide audience and tend to be up-to-date.

Cost will tend to be lower than for national training companies.

A linchpin of the nation's training systems. A wide variety of programs so you'll find what you need.

Training is usually specifically related to the business.

Programs speak to local concerns.

Programs are developed for specific groups of workers. Programs are usually convenient to attend.

Allows a designated employee to focus on worker training.

Allows people to learn at their desks and at their own pace.

Immediate help with new product. Often comes as part of package.

Commerce Dept. sponsors extension programs around the country. Many states run their own programs.

### DISADVANTAGES

Can be very expensive and may not be tailored enough to your business' or employees' needs.

Courses may not be sophisticated enough for your needs.

Courses may not be held at convenient times. Courses sometimes too academic.

Not all groups offer training sessions.

Programs may be too general or may be peripheral to your business.

Usually available only to union members.

Expensive to put someone on your payroll or free them from their normal duties.

Technology isn't always the best teacher. Can be expensive.

Trainers may not know your business and are limited in linking their products to other systems.

May not be located in your area. May be too focused on industrial production.

DATA: EDUCATION DEPT., LABOR DEPT., BUSINESS WEEK



in American work has led to a huge range of options for companies trying to get employees up to speed. Vendors and suppliers, chambers of commerce, government-sponsored economic development consortiums—all now offer technology education. Multimedia and online services as a teaching tool for high tech are starting to bear fruit. And importantly, community colleges have become the nation's technical training system. "Community colleges have been very responsive to what businesses and individuals need to work," says Anthony Carnevale, director of human resource studies at the Committee for Economic Development, a think tank in Washington.

High-tech equipment and investment in training is a sure-fire formula for a productivity revolution. Small businesses already generate more than half of all private-sector jobs. As they become increasingly dedicated to developing a computer-literate workforce, productivity growth, which has doubled in the 1990s from the anemic pace of the 1970s and 1980s, could keep climbing. Hard to imagine, but small business could become an even more formidable force in the economy.

**"HELP" FILES.** What kind of training makes the most sense for a smaller business? The cheapest and most common option is putting someone with technical expertise in charge. For example, although employees of PC Kwik Corp., a maker of software in Beaverton, Oregon, are technologically sophisticated, they still have to learn new programs all the time. "With a new technology, someone plays a lead role in learning it, and then they help others learn it," says General Manager Bruce Schafer. Because many small businesses have a fair amount of turnover, consultants suggest that the designated leader keep a record of frequently asked questions. These questions can be the basis of a "help" file for new employees.

Similarly, the New York City architectural firm Christidis & Lauster does most of its training in-house. Rather than wringing their hands during the real estate slump in the early 1990s, they used the time to test different soft-

ware systems and to focus on training. "When you have a lot of work and clients, it's very hard to make software switches and you have a lot less time to train," says partner Charles Lauster.

Another common approach is to get training from your computer or telecommunications vendor. Almost all the major players in these industries offer training services for their software. And in this era of corporate downsizing, when Big Business relies increasingly on smaller companies for services,

three half-day training sessions. But that wasn't enough, so Dawson also hired a systems administrator, at \$32,000 salary, to act as a computer mentor. The mentor/office manager stayed for 18 months and got 90% the system up and running. Productivity is up by about 30%, says Dawson, "because the computer system has cut down on the amount of time we have to spend on data. That's increased the time spent with the customer either on the phone or visiting with them."

In most parts of the country, the local community college or technical college is a rich training ground. Because they are local and practical in orientation, community colleges have turned out to be ideal partners for industries and local businesses trying to upgrade their workforce. Governments are using community colleges to reach small business. For example, the federal government in 1982 created the Manufacturing Extension Partnerships—modeled on the agricultural extension programs of the 19th century—to help small manufacturing businesses adopt new technologies quickly. Currently, there are 42 such centers around the country, typically tied to community colleges. Many states also have their own industrial extension centers and state-funded training programs.

When Frederick W. Taylor published *The Principles of Scientific Management* in 1911, he helped transform work by breaking every task into its simplest units. Taylor's methods soon became widespread among the nation's businesses and played a

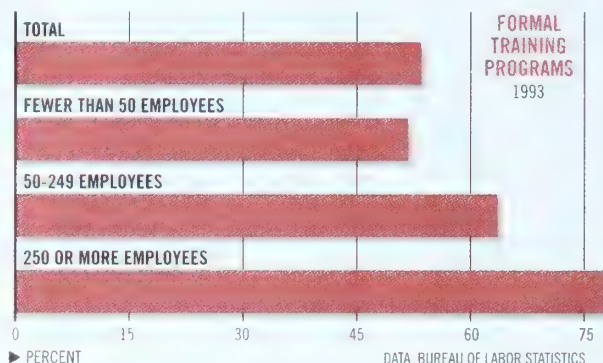
role in boosting U.S. productivity. But he also ended up eliminating learning from work.

In the Information Age, that separation is coming to an end. With computers, everyone is working more closely—manager and employee, producer and supplier, company and customer. In this economy, learning at work becomes a continuous process. But Taylor would not recognize the fruits of that change: higher productivity.

*By Christopher Farrell in New York with Ann Therese Palmer in Chicago and Gregory Sandler in Boston*

## Training In Corporate America

Surveyed companies that train employees to upgrade skills because of changes in technology and production methods



**CHANGING TIMES:** With computers, employees at all levels are working more closely—making on-the-job education a continuous process

the giants are offering training to their small suppliers. "Get the companies you sell to help you," says Carnevale. "There are many tricks to the training trade."

Many small companies aren't content with just one tack. Take Diane Dawson, head of Dawson Sales Co., a Chicago food ingredient broker. For some 35 years, the heart of the company had been a moving cabinet with hanging files where sales orders were kept. When Dawson bought a computer system (\$25,000 for hardware and \$10,000 for software), the package included



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# ZERO TO \$50 MILLION: NOW THAT'S MAGIC

Wizard's Magic is suddenly the top fantasy game for teens

It's a typical summer afternoon at Gary's Games, a small hobby store in Seattle. Outside, bikes are parked in a rack, while inside a mob of boys crowd around tables, dealing cards illustrated with mystical paintings. They have little interest in the traditional board games and puzzles that surround them. Instead, their minds are on mana, moxes, and a quirky place known as Dominia.

Sound bizarre? Not to the legions of 12-to-18-year-old boys who are as familiar with the terminology as past generations were with Boardwalk and Park Place. Mana is land, moxes are artifacts, and Dominia is an imaginary dimension where wizards cast spells and strange creatures roam. Together, they make up the fantasy world portrayed in one of the nation's hottest-selling games, Magic: The Gathering.

Thanks largely to informal tournaments like the one held at Gary's Games and the buzz that they've created, this deck of fantasy cards has become the top-selling adventure game, besting longtime favorite Dungeons & Dragons.

## ADVENTURE GAMES

Along the way, the owners of Wizards of the Coast, the tiny Renton (Wash.) company that invented and markets Magic, have felt some entrepreneurial enchantment of their own. Wizards won't discuss its finances, but industry insiders estimate that the company's sales totaled \$50 million in 1994, the first full year Magic was available. This year, sales could top \$100 million, figures the Games Manufacturers Assn. Not bad, considering that GAMA estimates sales of adventure games in 1995 could total \$750 million, roughly 60% of total game and puzzle sales.

Peter Adkison, Wizards' 33-year-old founder and chief executive, hopes to do even better, thanks to an arsenal of new products that capitalize on Magic's appeal. Already, the company publishes *The Duelist*, a bimonthly magazine chock-full of tips on game strategy.



In 1990, Wizards' founders were "playing" in a basement in a tiny Northwest town

Through joint ventures and licensing agreements, Wizards also sells paperbacks and comics based on Magic characters. Next year, a CD-ROM version of the game will be available from software maker MicroProse Software Inc. "The goal is to make games as big an entertainment as the movies," says Adkison.

While kids may be absorbed in Mag-

ic mania, some of their parents are up with the money they're spending on cards. A standard deck of 60 cards goes for \$8.95. But some are as rare as Mickey Mantle rookie card. A Black Lotus card, for example, fetches as much as \$300 on the black market. That's because only 1,100 were printed out of more than a billion Magic cards sold so far. Wizards says limiting the number of some cards encourages trading and enhances the game's appeal. But the company says that it never intended to turn Magic cards into just collectibles. To curb the fad, many school districts have put controls on playing Magic. Bedford, N. Y., north of New York City, students can play only if they have parental permission.

**GOING BOARDLESS.** The uproar has done little to dampen Adkison's glee over Magic's success. A former computer analyst at Boeing Co., he has been a fan of fantasy games since childhood.

Adkison founded Wizards in 1990 and moonlighted as a game developer. But nothing seemed to work until he met Richard Garfield, 31, another part-time game theorist, on an Internet game forum. At the time, Garfield was working toward his PhD in mathematics at the University of Pennsylvania. Adkison outlined his idea for a game using playing cards instead of cumbersome game boards.

Drawing on elements from previous card games he designed, Garfield needed a week to come up with a concept for Magic. The theme was simple: Players, or wizards, draw seven cards and shuffle their decks. Each

bears a mystical image and instructions on its powers. Artifact cards, for example, can depict weapons or spells to attack or defend. The goal: to eliminate your opponent's 20 life points and draw your adversary from Dominia.

The would-be game impresarios spent much of the next year in Adkison's basement testing Magic with friends and relatives. They sketched their controls on index cards and pressed the faces against copying machines to come up with contorted images to paste on cards. Once the bugs were worked out, they hired professional artists to draw cards, exchanging stock options in Wizards for their talents. Then the party along with friends and relatives, pool

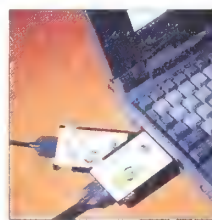
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# Companies

their savings to make prototypes that they exhibited at game fairs nationwide.

Within months, they snagged a big order from War Games West, a fantasy-game distributor in Albuquerque. The initial printing of 10 million cards in the summer of 1993 sold out in six weeks. Before long, Adkison had quit his day job. Today, Wizards has 260 employees, from artists to game designers, spread through two buildings in Renton. By cranking out a steady stream of new cards and powers, Wizards ensures that the games constantly change. And the

need to develop a strategy and play the odds has made the game a particular favorite of mathematically oriented, computer-savvy youngsters.

**ECCENTRIC ENERGY.** Like many small companies, Wizards has had its share of growing pains. Even though it has doubled its card output in the past year, Wizards admits that it can't catch up to this year's surging demand. Adkison recently hired Joiner Associates, a management consultant based in Madison, Wis., to advise him on better production procedures. Meanwhile, David Lewis was named Wizards' first chief financial officer last year. A 20-year business veteran who has worked at several Seattle-area companies, Lewis says the biggest challenge ahead is sorting out which opportunities to focus on. "We are in the middle of completing our first strategic plan," says Lewis.

Despite Wizards' growth, Adkison is determined to maintain its entrepreneur-



**CONJURERS:** Garfield and Adkison pooled their savings for Magic

rial spirit. He encourages a corporate culture that combines the intellectual nerdiness of a Microsoft Corp. with the uninhibited antics of a nursery school. Nerf wars occur daily. And it's not unusual to see staffers sporting costumes of Magic creatures, such as the goat-like Hurler Minotaur.

Tapping that eccentric energy is crucial if Adkison hopes to sustain Wizards' growth. Wizards' youthful audience isn't exactly known for its long attention span. Young boys are always looking for the latest fad—and they don't have to look far. Wizards' success has spawned over a dozen competing card games. TSR, the company that makes Dungeons & Dragons, makes two. Its most popular: Spellfire, another fantasy game that is as yet far less popular than Magic.

To help sustain Magic's momentum, Adkison is taking the game global. It's now available in seven languages, from Japanese to Italian. Wizards also entered

into a joint venture with Nightfall Games, a Glasgow-based game developer to extend Magic's appeal in Europe. And Adkison is counting on tournament play. In August, Wizards sponsored its second annual world championship in Renton, which attracted players from 19 countries.

Adkison is expanding Wizards' bag of tricks, too. Besides Magic, the company markets three other card games. And it has started selling board games, such as RoboRally, in which robots race along an obstacle course.

The new games are selling well, but none have cast the same spell on youngsters that Magic has. That has stirred speculation within the game industry that Adkison may be tempted to sell out to a manufacturer with the resources to finance a broad marketing push. Without naming any potential suitors, Adkison says he has been approached. But he insists he's not ready to sell. "I think we are just at the beginning of what we could do with the product," he declares.

Wizards could also raise capital by going public. Adkison says that's possible down the road. But, he says, Magic has strong enough cash flow to expand at a comfortable pace. He notes that Magic is now sold by major retailers, such as Toys 'R Us Inc. and software stores. That's far cry from hobby stores such as Games. If he can find even more outlets, Adkison may yet hold off the day that Wizards' magic wanes.

By Seanna Browder in Renton, Wash.

## Wizards' Growing Kingdom

**GAMES** In addition to Magic, the company markets three other card games. Soon to be released: NetRunner, where hackers and corporations vie for computer data. Has also begun selling traditional board games, such as RoboRally, in which robots race through an ever-changing obstacle course.

**BOOKS** Through a joint venture with HarperCollins, it sells a line of paperbacks based on Magic. Six have been published so far; three more are scheduled for release by February. The top-seller: *Forgotten Realms*, set in the multidimensional universe of Dominia.

**MERCHANDISE** Calendars, posters, pins, and T-shirts depicting scenes from its various fantasy games have been a big hit.

**OTHER** Publishes *The Duelist*, a bi-monthly magazine that offers tips on game strategy. Acclaim Comics publishes a series based on Magic that offers background on popular card characters. This fall, software maker MicroProse will start marketing a CD-ROM version of Magic. A video-game version based on the characters is also in the works.



**HAWKING WIZARDS AT A GAME CONVENTION**



# SING *CHI*—AND THE ET—TO REBUILD

y a quirky trouser retailer got back in business

digging out from disaster—it's a common experience for risk-taking business people. Few have had to do so literally as Seymour Ostrow. In 1994, the Santa Cruz, Calif. entrepreneur was running ChiPants Concepts Inc. By coming up with a catchy design and a New Age management, Ostrow had a thriving \$4 million pants business with seven Bay Area stores and an incredibly loyal following.

It took in a mere 15 seconds, all that was destroyed. The mammoth earthquake that tore through San Francisco destroyed Ostrow's business. Although his customers take their name from *chi*, a Chinese concept of "life-animating" energy, the 7.1-magnitude temblor packed more energy than ChiPants could cope with. Within a year, the financial aftermath turned his business into rubble.

**FIBER.** Now, the 46-year-old Ostrow is launching a comeback. But this time around, he's rebuilding through a different order and—with a jump-start from the Internet—he's off to a rapid start. *Chi* has returned," he says.

What's Ostrow's product? ChiPants are slacks tailored with a looser-fitting fit. A onetime teacher of yoga and a New Age "movement," Ostrow first decided a pair for himself: He wanted slacks with the comfort of sweatpants that could be worn to work. They quickly caught on among graying hippies, New Age devotees and so many Bay Area computer professionals that they became known as "hacker slacks." "I spend a lot of time sitting," says Palo Alto-based computer consultant Hugh Daniel. "They're the only pants I buy."

They also liked Ostrow's politically correct way of working: His stores were decorated in earth tones, hierarchy was ta-



## COMFORT ZONE

Ostrow—an erstwhile teacher of yoga—wanted trousers with the flexibility of sweatpants that could also be worn to work

boo among his enthusiastic young staff, and his pants were sewn locally using 100% natural cotton and hemp. Ostrow also adroitly marketed his Eastern-inspired philosophy, promising that the pants would help wearers free their own life energy. By late 1989, with monthly sales at 10,000 pairs, Ostrow had hired an outside CEO to manage growth.

But the quake had other plans. The Santa Cruz mall where Ostrow's flagship store was located was leveled, and his nearby corporate offices were condemned. His manufacturer was destroyed. With production stopped, Ostrow racked up \$500,000 in losses in less than two months. Short on cash, he shut his stores one by one. In July, 1991, he declared bankruptcy.

But in early 1994, Ostrow began traveling. From Japan to South Africa, he saw people in ChiPants and he learned

they still had a following. When he returned to California in late 1994, he dug out a customer list and started up again.

Ostrow began by calling his old customers and soon had orders for 120 pairs. He borrowed \$15,000 from friends and cut sample patterns. Then, Ostrow's renewed *chi* really kicked in: In search of a manufacturer that would make a small, 400-pair run for him, he called an old supplier: Seymour Jaron, owner of SJ Manufacturing Inc. in San Francisco. For a plant that normally makes orders of 10,000 or more, that was a money-losing proposition. But Jaron remembered ChiPants—and owned a pair. He and another investor decided to buy a 20% stake in Ostrow's new company.

**FLOODED.** More good fortune followed. A fan posted a message on the WELL, a popular online service, announcing ChiPants was back in business. Ostrow was flooded with E-mail asking where to buy them. Although he had planned to sell only through mail order, Ostrow realized his niche customers were more computer-literate than most. He drew up an Internet marketing plan and got a friend to create a site on the World Wide Web.

Hundreds of browsers now look at the site daily. Ostrow can't yet take orders online, but customers can download order forms or request swatches of ChiPants' fabrics. More important, Ostrow is rapidly building a customer list at a fraction of the cost—and time—that more traditional methods would have taken. "It's electronic word of mouth," he says.

Still, Ostrow has a long way to go. Margins remain slim, and cash flow tight. With a new mail-order catalog due out in October, monthly production will hit 3,000 pairs. By spring, Ostrow aims to be back to 10,000 pairs a month. And with no patent, anyone could copy his pants if he does succeed. But for now, Ostrow has little time to worry about rivals. "I'm just trying to grow this company in doable steps," he says. Presumably, he's wearing the loose-fitting garb that will make those steps comfortable.

By Julie Tilsner in New York

## COMEBACKS



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# NETWORKING: A GIANT STEP FOR THE SMALL

Getting wired can be daunting, but even a one-person operation can reap big benefits

**A**gents at Kim Dawson Agency Inc. in Dallas used to tack elaborate flow charts, each 2½ feet long, to the office wall to keep track of which of 115 models were hired for particular fashion photo shoots. The decidedly manual system forced agents to wander around the room when booking models, often stumbling over telephone cords, checking a dozen different charts to make sure a model wasn't committed. Now and then, though, agents double-booked, forcing embarrassing cancellations later.

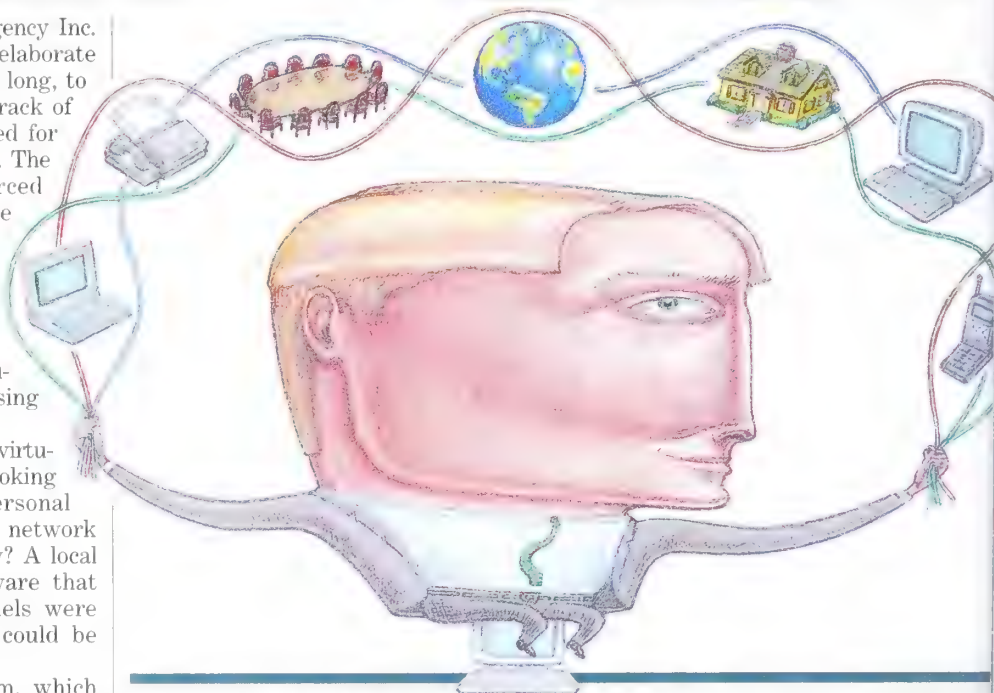
In 1991, though, the agency virtually eliminated the double-booking problem by installing 12 personal computers and a Novell Inc. network that linked its 11 agents. How? A local programmer developed software that checked to see whether models were already booked before they could be committed to a job.

The benefits of the system, which cost the agency \$50,000, didn't stop there. Computer systems manager Tammy Meche says the network, which also allows agents to do bookings faster, has helped Dawson push sales up more than 50% in the past four years, to a projected \$8 million in 1995—without adding any new agents. Says Meche: "We probably couldn't have done it without the network."

**NETWORKING**

The lesson? Networking technologies—local-area networks (LANs), client-server systems, electronic mail—aren't just for big companies. Businesses as small as a single-person shop can reap tremendous benefits, including faster time to market, higher productivity, and closer contact with customers, by drawing on the same communications infrastructure that companies such as 3M, Citibank, and Caterpillar have deployed. It's possible to become wired for as little as \$100—or as much as \$500,000—depending on your ambitions.

Getting the technology right is never easy, but it can be especially daunting



## Tools for the Information Age

### LOCAL-AREA NETWORKS

If the business is big enough to have several computers, link them together in networks that allow co-workers to easily share information and computing resources.

### PORTABLE COMPUTERS

Notebook computers can keep the salesforce plugged into the home office. Handheld data terminals and personal digital assistants can be had for a few hundred dollars and can be used by low-skilled workers to gather data in the field.

### E-MAIL

A cheap and easy way to stay in touch with customers and suppliers. Small businesses can buy electronic-mail services from telephone companies or use the Internet through a variety of providers including online services such as CompuServe, America Online, or Prodigy.

### FAX

Don't want to stand at the fax machine all day sending faxes? Convert a PC to a "fax server" that can do the job of a dozen separate fax machines—and relay incoming fax messages to any computer on the network. An alternative: use a fax service such as AT&T Mail to do the job for you.

### GROUPWARE

Even a small business with 100 to 200 employees can benefit from groupware programs such as Lotus Notes. It's a good way for employees to swap information and collaborate.

DATA BUSINESSWEEK

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# Technology

for small businesses. Many smaller companies don't have the in-house talent to get wired and keep a network humming. Or top management may be so swamped with other problems that it can't spare the time to learn the benefits of network technology. And small businesses have little margin for error: A botched network project that might cost a big corporation a penny of quarterly per-share earnings could wipe out a small one. So it's no surprise that many small businesses simply avoid thinking about networking. That could be a big mistake, says Clark Witmer, vice-president for logistics at Morton Metalcraft Co., a \$55 million sheet-metal fabricator in Morton, Ill.: "Small businesses won't grow these days unless they construct the right technological platform."

When it comes to getting networked, in fact, small businesses can have some big advantages. In many cases, a small outfit hasn't been using technology for long, so it "doesn't have to plan around

Koch \$200,000, but it allowed the company to choose and customize a software package that has dramatically boosted the number of orders it can process in a day—to 50,000 from 1,000. Vice-President John Starr figures the system will cut inventory costs by \$100,000 annually and save \$100,000 in labor costs.

Still not ready for such a big commitment? You can still get started in networking—by simply opening an E-mail account. E-mail and fax services allow small companies to vastly improve their contact with customers and suppliers. Sharper Finish Inc., a \$4 million Chicago manufacturer of commercial laundry equipment, uses AT&T Mail to fax delivery schedules, product announcements, and price information to its 175 worldwide distributors. Before signing up for the service last year, the company typed up newsletters and sent them via mail or fax. Now, an assistant types a newsletter into a computer and sends it out over the AT&T network. "We get

which conducts food-safety inspection for restaurant chains, including Tac Bell, equips each of its 120 inspectors with a Newton handheld personal digital assistant from Apple Computer Inc. and a Canon Inc. printer. The combination allows the inspector to print a report on the spot for restaurant managers, enabling them to address any problems immediately. In the past, when inspectors used multipage forms, it took several days to get out a report.

**MORE SUPPORT.** Still, adopting networking technology doesn't necessarily lead to corporate nirvana. It's easy to stumble. When Chicago-based Assist Network Development Inc., an installer of computer and telephone cabling, decided it needed to get more data to its nationwide offices, the company installed Lotus Development Inc.'s Notes, a popular groupware software program that allows people to work together on documents and schedules. But the company, which expects to post sales of \$10 million this year, budgeted only \$50,000 for a project that has now eaten up over \$300,000 and taken nine months. The problem? Executives became enamored with Notes capabilities that they kept ordering consultants to write more applications for them. "We didn't have proper controls," says CEO Stephen Watkins.

In general, groupware presents big networking challenges for small business. Most groupware systems require admini-

## NET GAINS: Good planning is essential, and small fry have some advantages in communications. Unlike big companies, for example, they don't have to deal with a mass of old, outdated equipment

an installed base," says Andersen Consulting networking specialist Christopher Teeter. That means smaller companies can buy what works best for them without worrying about the thorny network-integration questions that bedevil large corporations with "legacy" computer systems. And lack of knowledge about how to install the system isn't the drawback it once was: There are thousands of small consulting firms and lots of network-literate college graduates to help out—for a price, of course.

**CUSTOMIZED SETUPS.** Good planning, though, is essential. Just ask Koch Supplies Inc., a \$70 million manufacturer and distributor of butcher supplies based in Kansas City, Mo. When Koch needed new software to run its network—which handles everything from order entry to shipping—the company hired software maker J.D. Edwards & Co. to do a needs assessment and pulled in Arthur Andersen to run software trials. The selection process alone cost

information into our distributors' hands much more quickly now," says Vice-President Craig Roberts.

So what kind of network is the right kind? That depends on what a business wants to do. Simple E-mail is a must for a one-person office, while a LAN could be important in a business with as few as three employees where co-workers need to share information. Mark Ingwer, a consultant who does market research for telecommunications companies, uses CompuServe Inc.'s E-mail service to send proposals and queries to clients. CompuServe, which costs him \$10 a month, also gives him access to the information-rich Internet. Recently, he pulled information on what the optimal applications are for wireless data communications off the Net. The information he has gleaned from the Net, he says, "has helped me put together some smart proposals."

Small businesses don't have to shy away from more sophisticated technologies, either. Audits International Inc.,

trators to keep them current—and stop them from running amok. That adds a layer of cost that small businesses need to consider, says Todd Miller, partner in Revere Group, a computer consulting firm in Northbrook, Ill., that put in its own Lotus Notes system last year. The system's complexity forced the firm, which is 100 consultants strong, to hire extra support staff. "It's an inevitable and necessary evil," says Miller.

But would Miller junk his system? No way. He says Revere consultants now use the Notes system to swap information that allows them to solve thorny issues and write better proposals—just like bigger rival Andersen Consulting, whose Notes-based system is one of the industry's best. And that may be the ultimate benefit of networking technology for small businesses: It gives them many of the resources their bigger rivals, without all the baggage that comes with size.

*By Kevin Kelly in Chicago*

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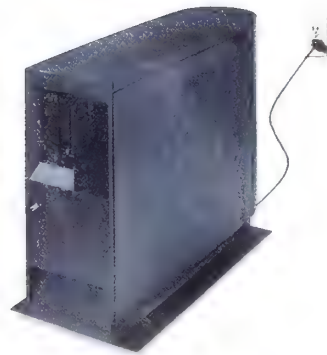
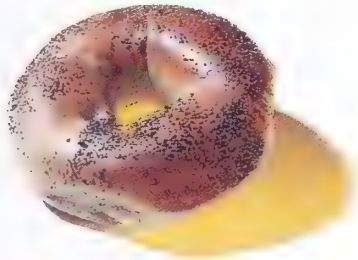
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Solutions for a small planet



# WHY JAPAN HASN'T CAUGHT SMALL-CAP FEVER

Strict rules and a preference for the tried and true make startup funds hard to come by

It's the sort of outfit that investment bankers love to take public. Tokyo's Impress Group has 10 computer and music magazines, including Japan's first Internet title, a flourishing CD-ROM business, and even a popular Godzilla screen-saver. Thanks to the current boom in personal-computer sales in Japan, Impress, with sales of \$49.4 million, predicts its earnings will rise 54% this year, to \$3.7 million.

So is founder and self-proclaimed computer nut Keiichiro "Ken" Tsukamoto, 38, tapping Japan's \$4 trillion equity market to bankroll expansion plans into Internet home-shopping? Probably not. Tsukamoto launched his business in 1991 by using revolving bank credits and by dipping into the \$150 million in stock he carried away from ASCII Corp., another computer-magazine publisher he helped found. "I was very lucky," he admits. But given Japan's stringent listing requirements—plus investor jitters about the country's economic prospects—all he can do right now is dream of selling new shares to the public. "We would like to go public," says Tsukamoto, "but it's unlikely, be-



**TSUKAMOTO:** "Publishers aren't really considered financially secure"

cause publishers aren't really considered financially secure."

**HIGH HURDLES.** Indeed, Japanese growth companies such as Impress have to survive pretty much by their own wits—and often from their own pocketbooks. Only those with \$2 million in equity and a year's worth of profits before listing

have been able to come out on Japan's over-the-counter market. Rules are even tougher on the Tokyo Stock Exchange's second section, where midsize companies trade. Second section issuers must have \$10 million in equity and three straight years' profits to gain listings.

Few startups can make it past such formidable obstacles. That's why the average age of companies listing on the OTC market is 20 years, vs. 5 for America's NASDAQ. Worse, Japan's venture-capital market has declined as the economy has tanked, falling from \$9 billion in 1992 to about \$6 billion in '95.

The dearth of funds has sent some companies abroad in search of cash. Kobe's Muramoto Industry Co., a maker of chassis for videocassette recorders, went to the Thai stock market to raise \$2 million for a plant near

Bangkok. Other outfits such as Biomaterial Co., a high-tech specialist in cell-based materials, have even considered seeking a NASDAQ listing.

That small companies are largely shut out from raising capital in Japan is becoming a concern for policymakers trying to pull their country out of its long

## The Struggle for Cash Among Startups

DATA PROVIDED BY

### FRONTIER MARKET

Starting in November, small companies with no profit track record can list on this new market.

Downside: Disclosure requirements too skimpy to lure most investors.

### TOKYO STOCK EXCHANGE

TSE may launch second section for small-cap stocks in 1996. Will attract some companies with proven earnings records, but other promising ones won't qualify.

### VENTURE CAPITAL

A slew of funds has come online, but overall venture capital has declined since 1992. Commercial banks will lend only in small amounts to no-name entrepreneurs.

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**OHKI OF NIPPON LSI CARD:** "Japanese investors expect sure returns"

economic slump. With large manufacturers laying off workers at home and moving production offshore, any new jobs that Japan Inc. creates are likely to come from smaller fry. Yet they're starved for capital. "This is the first time I've seen the number of business failures exceed startups," laments Ryutaro Hashimoto of the Ministry of International Trade & Industry (MITI).

Still, there are signs that the capital squeeze may be easing. When an economic recovery looked as if it was beginning last year, Tokyo's second-section index vaulted 30% at one point. When the recovery fizzled, so did the index, which is currently about 40% of its 1995 peak. Now, with equities recovering, as interest rates fall and as the yen's strength ebbs, a slew of small-company funds is emerging. Daiwa Securities Co. and Yamaichi Securities Co. have raised about \$300 million for their venture funds. Nomura Securities Co.'s Jafco unit has taken 20 companies public since April.

**MOUNTING PRESSURE.** Trouble is, companies that do gain listings are big and established by U.S. standards. And the economic signs point to even more pressure on small companies. Brutal cost-cutting campaigns by big Japanese com-

panies mean they are dumping smaller suppliers at home for more affordable Asian counterparts. In addition, a flood of cheap imports—everything from European lager beers to Armani suits—has touched off widespread "price destruction" that's battering the lower end of the corporate chain. "Small and medium enterprises are where the brunt of the restructuring is taking place," says Morgan Stanley & Co. economist Mineko Sasaki-Smith.

To help out, MITI guaranteed more than \$200 million in small-business loans in 1994, and plans to step up aid this year, particularly to promising high-tech-

**BRIGHTER OUTLOOK?**  
As interest rates fall  
and the yen loses  
some of its strength,  
the capital squeeze  
may be easing up

nology companies. MITI also led a mission to the U.S. to study NASDAQ. A new stock market—dubbed New Frontier—aimed at nourishing young companies with risk capital, will start trading in November.

MITI and the Ministry of Finance promoted the idea without first consulting Japanese brokers, who contend that most conservative Japanese investors won't go for the shares of unseasoned startups with no record of profits. Brokers are insisting that New Frontier companies come up with audited financial statements as the price of listing.

A more promising avenue for new listings might be a plan by the Tokyo Stock Exchange to start an offshoot in its second section—one with looser listing requirements. "A lot of companies could go right on that list," says Paul Heston, a venture-capital analyst at Deutsche Bank. The market won't get under way until 1996 at the earliest.

So it may be some time before Japan catches the kind of small-cap fever that has fired markets in the U.S. While the Nikkei stock average has recovered this year to the 18,000 level, that's only half its record level of 1989. And most Japanese investors, having been burned, are sticking to blue chips. "Japanese investors expect sure returns," says Shinji Ohki, president of Nippon LSI Card Inc., which is developing a digital camera that can take pictures, store them, and transmit them over a telephone line.

Of course, companies deemed strategically important by MITI are getting helping hand. Take the Japan High-Tech Satellite Network, whose parent company, JTAS, is 60%-owned by MITI and other companies such as NEC Corp. and Matsushita Electric. MITI sees JTAS, producer of scientific videos, as a promising entrant in the global multimedia boom. The official blessing helped JTAS raise \$5 million in startup money in 1994. It will get an additional \$2 million next

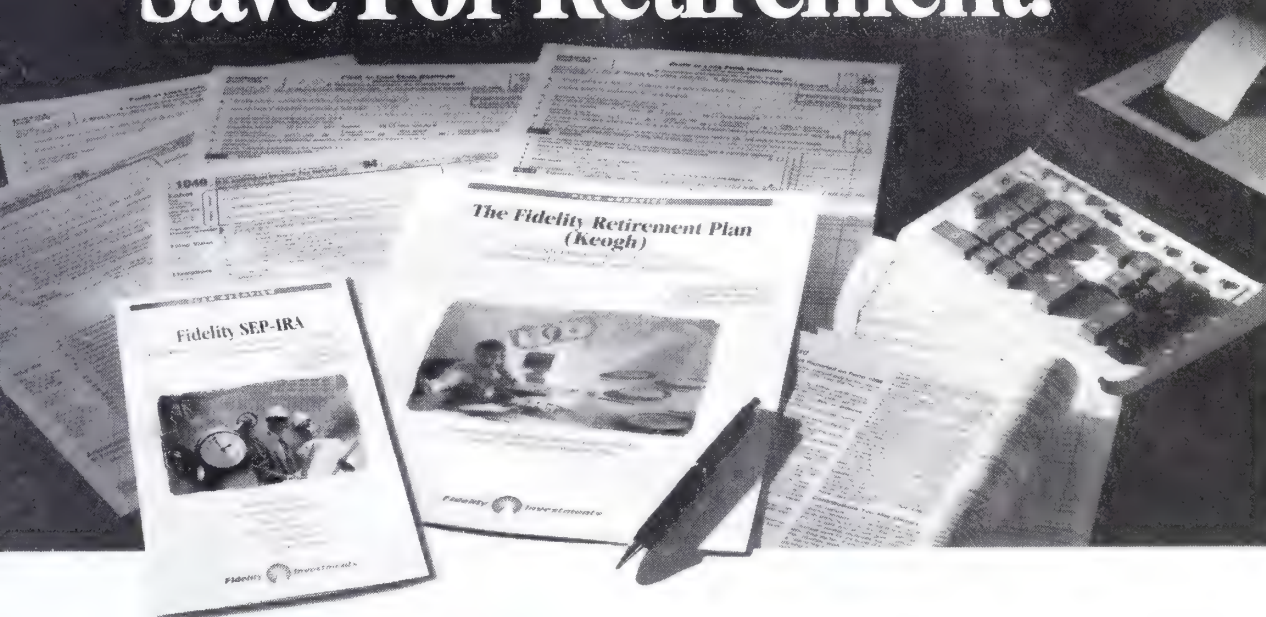
month from the government agency to launch an ambitious project to download its video by satellite to university and business users in Japan and elsewhere in Asia. But most of Japan's small companies, long on promise but short on profit, are pretty much on their own. Until Japan has something like a NASDAQ that rewards investors who bet correctly on the next Sony Corp., the nation's entrepreneurs face an uphill battle for cash.

By Brian Bremner in Tokyo



*Advantages For Small Business Owners*

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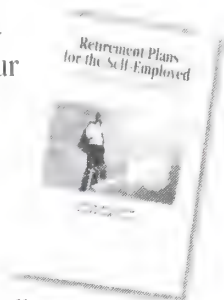
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# WHO SAYS WASHINGTON IGNORES SMALL BUSINESS?

Conference organizer Alan Patricof sees a brightening picture

**A**s the overseer of \$2 billion in venture-capital investments, Alan J. Patricof didn't need anything else to do. But for the past two years, he has spent his downtime organizing the White House Conference on Small Business, a process that drew together more than 20,000 small-business people, culminating in a Washington meeting in June. The result: 60 proposals that have been forwarded to Congress for consideration. Here's what Patricof told Assistant Managing Editor Sarah Bartlett and Department Editor Amey Stone about the conference and the state of small business:

**Q:** Now that you've recovered a bit, was it all worth it?

**A:** Everyone told me that the 1986 White House Conference on Small Business was a very big disappointment, because the President and the Vice-President were both out of town. In fact, it was held during the summer recess, so Congress wasn't even there. Everybody remembered the fact that there had been no real participation by the government. And small business really was very negative and skeptical... I think the fact that the process worked this time [both the President and Vice-President attended] was a major accomplishment. I think a lot of people became more comfortable with the whole Washington process and found out that it's more user-friendly than they realized and that a lot of things are possible.

**Q:** What in particular do you think has gotten better?

**A:** I think there have been improvements—dramatic improvements—in regulation and paperwork. You know, it's very hard when you're a small business used to complaining and wanting to im-

pact change, to recognize that some of the changes have already taken place, or that legislation may have passed already. For example, the President passed the targeted capital-gains bill, which reduced the capital-gains tax by 50% on investments in small companies. Well, people were complaining all through the conference—not complaining, recommending lowering the tax for investing in small compa-

## ISSUES & TRENDS



nies. But they have it already! Now, whether they're using it, that's another matter... The same thing with regulation. There has been a lot of reduction. I mean a lot! The most significant reduction has been in the banking area. At the direction of the President and also on his own initiative, the Comptroller of the

Currency has been reducing paperwork for getting loans, so you don't have to go through three different agencies and you don't have to get an appraisal on your house. Things like that.

**Q:** What is your sense of how competitive America's small-business sector compared with Europe's or Asia's?

**A:** Oh, I think we're way ahead. The mentality of the entrepreneurial motivation in this country is far beyond what it is anywhere else in the world—because failure is more acceptable here. You can fail and start again here much more easily than you can in Europe—although it's better there than it was 20 years ago. Today, you start up, you raise money, and if the company fails, you end up owing the bank money, and nobody likes to do that. But you can go back again and start again, whereas in Europe if you fail, it's very hard to do it a second time.

**Q:** Given how much time you've spent chairing the White House conference, how's your own business doing?

**A:** My business [Patricof & Co. Ventures] hasn't suffered. We have over \$1 billion, of which \$700 million is in the U.S. Our portfolio here tends to be more broadly diversified. In Europe, for instance, our funds invest much less in the type of entrepreneurial startups that we do here. Here we're investing in health care technology, and retail concepts. And we invest not just in early-stage situations; we do early-to-later-stage. In Europe our investments are more in later stage, consumer-type industries. It's really almost restructuring the middle size, family-size companies that are taking in outside capital and expanding.

**Q:** How have the returns on your fund been?

**A:** We have an annual 35% net internal rate of return, which is very unusual in the U.S. And that's a fund that's now almost seven years old. We've had several successes in that fund, but high tech has been part of it and so has retail. In Europe, our return has been closer to 18% to 20% net a year.



# 'NEW-GIRL' NETWORK STARTS TO TAKE ROOT

From SBA loans to tech support, female entrepreneurs are finally getting respect

After Michelle Berry was fired in 1993 from her sales job with a coffee equipment distributor, she borrowed \$15,000 from family and friends and pluckily started her own business reselling espresso machines to restaurants, hotels and stores. Two years later, Java Traders is nearing \$1 million in sales, and Berry needs more employees to increase inventory.

Against-the-odds success story? No thanks to local banks, who shunned her, says the 30-year-old Arvada (Colo.) resident. "I was too young of a woman in a male-dominated business," she says. Berry hadn't been in business long enough, banks said, her assets weren't enough. Luckily, Women's Equity Fund

(WEF), a Denver-area venture-capital fund, came to the rescue with venture financing, a guarantee for a bank loan—much more. WEF helped her computerize, hire a bookkeeper, and market her products. "Any question I have, they're there to support me," she says. Raising money for small businesses is no easy thing for any entrepreneur, but, as Berry learned, it's particularly vexing for women. Although they own 40% of U.S. businesses and start them

as often as men, women have not been welcomed by traditional sources of financing such as banks and venture capitalists. According to a recent study by the National Association of Women Business Owners (NAWBO), 52% of women entrepreneurs turn to credit cards to finance their businesses, vs. 18% for all businesses.

But, the path to financing is widening.



**BERRY:** Shunned by banks, rescued by Women's Equity Fund

More banks are lending to small business, and a few venture firms are targeting female entrepreneurs. The Small Business Administration rolled out some programs that facilitate lending to women, and organizations are surfacing to offer technical support for women to start, run, and expand their businesses.

That's a turnabout for many banks, which have eschewed small firms. The interest on loans of less than \$50,000 usually doesn't cover the processing costs. And banks' lending criteria, often tailored to larger companies, frequently don't apply. Worse yet, because they predominantly start service businesses, women often lack the hard assets banks require for collateral. And, according to NAWBO's study, one-third of women entrepreneurs still "perceive some degree of gender-based dis-

crimination from their financial institution."

But moves are afoot to lower the banking barrier. On Sept. 20, Wells Fargo & Co. announced a new \$1 billion fund to lend expansion funds to companies owned by females. "Women-owned business is a large and growing market," says Terri Dial, executive vice-president of the Business Banking Group at Wells Fargo, "and it's not well-served." Borrowers need good personal and business credit and to have been in a profitable business for two years. At least one other bank, Harris Bank Corp. in Chicago, has formed a unit solely to lend women amounts ranging from \$10,000 to a few million.

Wells, the largest lender to small business, cut the cost of such loans by automating the process,

screening for promising recipients, and sending out a direct mailing of prequalified loan applications—the way banks do with credit cards. Other banks, such as Bank of America Corp. and PNC Bank Corp., have boosted small business lending.

**NEW INITIATIVES.** Many entrepreneurs have turned to the SBA, which guarantees 70% of a bank loan. But although women have been starting businesses in record numbers, until 1993 they were getting only 8% of SBA-guaranteed loans. The SBA raised that percentage to almost 25% by 1995 with new initiatives such as the Women's Pre-Qualification and Low Documentation loan programs. Through the former, in effect in 16 cities, the SBA gives a preliminary commitment to guarantee a loan before the entrepreneur approaches a bank. What has made the biggest difference, says deputy administrator Cassandra Pulley,

## WOMEN ENTREPRENEURS



is a simplified, low-documentation process for loans under \$100,000. The old 12-page application has been replaced by a one-page form. "That made it a lot easier for banks to process the loans," she says.

Venture capital is the toughest source of financing for entrepreneurs to crack, because investors covet rapidly growing companies in areas such as high tech that can deliver better-than-market returns. But two-thirds of women-owned businesses remain in low-growth areas of retail and services. Moreover, the venture community has always been clannish. Of the 2,000 professionals in venture-capital firms, fewer than 50 women are decision-making, deal-doing partners, according to Sona Wang, a principal at Inroads Capital Partners, a \$50 million Evanston (Ill.) fund. "A lot of guys know how to get on the network," says NAWBO's venture-capital liaison Beth Kljajic, who has started several businesses of her own. "I didn't even know the network existed—and there's no women's version."

But some are trying to redress this problem. Inroads Capital looks for women- and minority-owned businesses, which are "vastly underserved by the institutional marketplace," says Wang. It funds companies with several million dollars in revenue that want to raise \$1 million to \$10 million. Other venture groups targeting women include Denver-based Women's Equity Fund, which has raised \$750,000 in equity financing and is working with the Bank of Boulder and Norwest of Colorado to provide debt financing as well. President Annette Taylor



**O'ROURKE:** An AWED connection led to a \$75,000 loan

thinks investing in women-owned businesses gives WEF an edge: It's a "niche market that has not already been exploited," she says. And Blue Chip Venture in Cincinnati has a \$15 million opportunity fund designated for women and minority-owned businesses.

Also promising for startups is Chicago-based Investors' Circle, a nonprofit network of investors who invest in socially responsible businesses, including many owned by women, says Executive Director Susan E. Davis. Women entrepreneurs submit a company description that is circulated to 150 potential investors nationwide. "Our members invest in seed stage, startups, expansion, and mezza-

nine-level financing," says Dav

Two other organizations are addressing another perennial problem for women entrepreneurs: the lack of collateral. Women Inc. in Long Beach, California, steers members to a \$150 million loan pool from the Money Store Inc., an official SBA lender which uses the Low Doc program to qualify loans on the basis of personal credit, the business plan, and the ability to repay from cash flow, rather than collateral. Women Inc. also provides referrals, technical support and benefits such as health care and discount business services for a \$29 annual fee.

Likewise, Women's Collateral Funding in Philadelphia is raising a million dollar fund to buy collateral that serve as collateral for female entrepreneurs who have none, but otherwise would qualify for bank loans. In exchange, WCF takes a small equity or realty stake in the company.

**SKILL SHARPENERS.** Probably the biggest financial barrier for women even those with an intricate knowledge of their own businesses—remains their ignorance about how to craft a business plan, make projections, or seek outside financing. However, many organizations exist to teach these skills. The American Women's Economic Development Council (AWED) in New York, Los Angeles, and Washington, the Women's Business Development Center in the Midwest, and NAWBO all provide referrals or classes on how to get financing.

So it appears that a "new-girl" network is finally starting to take root. Consider Nancy O'Rourke. After her divorce in 1990, she wanted the flexibility to raise her two children while she worked. The Long Beach (California) singer started Mr. Cat Productions, supplying and operating sound equipment for concerts and speeches. In the beginning she financed the company from her job to job. In 1993, she took an AWED course called Managing Your Business and learned crucial skills in recordkeeping and targeted marketing. She also compiled a two-inch-thick business plan. At AWED she met Executive Director Judith Luther Wilder, who soon left to start Women Inc. That's how O'Rourke found out about the Money Store and got the \$75,000 loan to expand into recording sound equipment. For her, the network is already paying dividends.

By Pam Black in New York

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800 359-3557 ext. 120 Operates a \$1 billion loan pool for women with established businesses and good credit

#### WOMEN INCORPORATED

800 930-3993 \$150 million loan pool, health plans, credit cards, and other service (membership \$29)

#### WOMEN'S COLLATERAL FUNDING

215 712-1900 Guarantor/partner for women who are turned down for bank loans only because they don't have collateral

### VENTURE CAPITAL

#### WOMEN'S EQUITY FUND

303 443-2620 \$750,000 fund; also offers loans with local banks

#### INROADS CAPITAL PARTNERS

708 864-2000 \$40 million fund; backs established businesses

#### INVESTORS' CIRCLE

708 876-1101 Circulates summaries of businesses to 150 prospective investors

#### BLUE CHIP OPPORTUNITY FUND

513 723-2300 \$10 million fund; targets women and minorities

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| Compatibility: | PCs and MACINTOSH<br>computers               | Flash:     | 4 to 9 feet  |
|                |                                              | Batteries: | 4 AA lithium |

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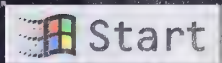


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# PHONE BREAKS FOR SMALL BUSINESS

Resellers can save the little guy a bundle on long distance

**A**mong all of the concerns of small-business owners, shopping for long-distance service might not rank very high. Sure, small companies want the lowest possible rates without sacrificing quality, and they covet 800 numbers, calling cards, and all of the other services that big businesses take for granted. But few modest-size enterprises can afford a dedicated telecommunications staff, and most have been happy to take what they can get from AT&T, MCI, or Sprint—even if better deals could be found elsewhere.

Enter telephone resellers—about 800 companies that primarily cater to small and midsize businesses. Rather than building their own networks, resellers purchase bulk long-distance capacity at wholesale prices from major carriers, then resell the service to small businesses at discounts of 10% to 35%. "A small-business person who wants to save on their phone bill should immediately look beyond the top three," says Robert Rosenberg, president of market researcher Insight Research Corp.

**HYBRIDS.** The major carriers and resellers are partners and enemies at the same time. Indeed, the largest long-distance companies—the Big Three, plus WorldCom, Frontier, and LCI International—are hybrids that routinely sell directly to customers in one area while going through resellers in others.

Regardless of who owns which piece of what network, long-distance service has become a commodity. Virtually all carriers employ fiber-optic cable and digital switches and at times route calls through other carriers' lines. What matters, then, is the level of customer service a reseller (or major carrier) can provide, the features

it offers, and, of course, the cost.

As usual, read the fine print, and if you haven't heard of a carrier, check references and call the Better Business Bureau, or state regulatory commission. You can also contact the Competitive Telecommunications Assn. or the Telecommunications Resellers Assn., both Washington-based industry groups.

Many resellers try to get to know their customers. Seattle-based MIDCOM Communications dispatches a personal representative in 20 cities to clients who bill more than \$500 a month. MIDCOM's rep can go over a phone bill to determine, for example, whether it would be cheaper for a company to put in an 800 number rather than to have its sales

force continually phone in using cos calling-card rates. Bill O'Bryan, the owner of a swimming-pool business in Louisville, switched to UniDial Communications, a reseller (using WorldCom Inc. WiTel network) because of its personalized service. Once a customer of AT&T, MCI, and Sprint, O'Bryan is charged about 12¢ per minute by UniDial, down 25% to 30%, he says, from what Big Three charged.

UniDial's plans are fairly representative. The company's

Plus service is designed for businesses that spend more than \$250 a month on long distance. It features

hour customer service, flat rate billing, and no startup fee. Customers are billed in six-second increments—after an initial 18-second period for domestic calls. Steer clear of companies that bill businesses in anything greater than six-second increments. By contrast, residences usually are billed in one-minute intervals.

In choosing any carrier, Robert S. president of Market Dynamics, Bethesda, Md., publisher of *Dr. Bob's Long Distance For Less* rate guide, advises owners to dissect their most recent phone bills. How many calls a minute do you make to a satellite office or area of the country? Do you pho

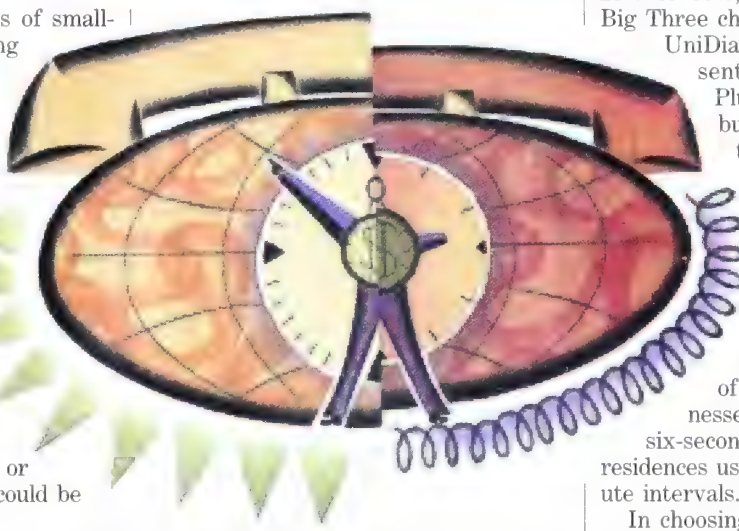
## TELECOMMUNICATIONS

overseas? Then, carriers slug it out over a pricing plan that best suits your business' calling patterns.

One warning: If you make a lot of international calls, you might want to consider one of the Big Three or a late second-tier international carrier, advises Robert Mirani, senior telecommunications analyst at Yankee Group Inc., Boston. Smaller resellers, he says, may not provide much of a break on overseas calls.

Resellers should also provide detailed billing reports, such as a list of 10 longest calls made during a month and the most frequently dialed area codes and numbers. Who knows? If you identify an employee who abuses your good graces by calling out-of-state cronies, you might save even more money than you were banking on.

By Edward C. Blum  
in New York



## DIALING FOR DEALS

*If you're considering a reseller, homework is in order:*

**SCRUTINIZE** your previous bills to determine your long-distance and overseas calling patterns.

**CHECK** to make sure that you are billed in six-second increments, and compare minimum fees for short calls.

**DETERMINE** whether a reseller offers enhanced billing reports, from detailed accounting codes to frequently called numbers.

**FIND OUT** its customer-service hours and whether you can deal with a specific customer-service representative.

DATA BUSINESS WEEK





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## TRUE GRITS

**F**ew things are more annoying than a government regulation that consumes time and energy but seems to serve no useful purpose. In that spirit, BUSINESS WEEK is launching Wit's End, a new feature that shines a light on some of the peskier regs out there that make you scratch your head, exclaim in horror—or, depending on your sense of humor, laugh in disbelief.

Our first in this series is drawn from a Food & Drug Administration/Agriculture Dept. regulation dating back to 1977 that dictates what food companies can label and sell as grits. This particular piece of oversight was uncovered by Vice-President Al Gore's office as part of his effort to streamline government. It is scheduled for demise—but that still leaves plenty of other grist for this mill.

Grits, corn grits, hominy grits is the food prepared by so grinding and sifting clean, white corn, with removal of corn bran and germ, that on a moisture-free basis, its crude fiber content is not more than 1.2% and its fat content is not more than 2.25% and when tested by the method described in paragraph (b)(2) of this section, not less than 95% passes through a #10 sieve, but not more than 20% through a #25 sieve.

Paragraph (b)(2): Attach bottom pan to a #25 sieve. Fit the #10 sieve into the #25 sieve. Pour 100 grams of sample into the #10 sieve, attach cover and hold assembly in a slightly inclined position. Shake the sieves by striking the sides against one hand with an upward stroke, at the rate of about 150 times per minute. Turn the sieve about one-sixth of a revolution, each time in the same direction, after each 25 strokes....The percent of sample passing through a #10 sieve shall be determined by subtracting from 100% the percent remaining in the #10 sieve. The percent of material in the pan shall be considered as the percent passing through the #25 sieve. (21 Code of Federal Regulation, Section 137.230)



**GOT A CANDIDATE FOR WIT'S END?** Readers should send them to Business Week Enterprise, 1221 Avenue of the Americas, New York, N.Y. 10020, fax (212 512-4721), America Online (readersbw), or Internet (bwreader@mgh.com).



# BusinessWeek

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Would you please tell us what you think about Enterprise? Just fill out this quick one page "Fax-Back" survey and give us your opinion. Fax it to 516-935-4092. If you do not have access to a fax machine, you can mail this survey to: Ms. Patrice Serret, Business Week Enterprise, 1221 Avenue of the Americas, 40th floor, New York, New York 10020.

**1. Would you say the editorial content of Enterprise was:**

- ☐ Excellent
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- ☐ Good
- ☐ Fair
- ☐ Poor
- ☐ Don't Know

**2. Did you find Enterprise: (Check all that apply)**

- ☐ Comprehensive
- ☐ Concise
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- ☐ Informative
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- ☐ Interesting
- ☐ Pertinent to my business needs
- ☐ Useful
- ☐ Well organized
- ☐ Other \_\_\_\_\_

**3. Next to the editorial subjects listed below, please check those topics which you would like to see more of in Enterprise:**

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- ☐ Economic conditions
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- ☐ Industry trends
- ☐ International business
- ☐ Legal issues
- ☐ Marketing
- ☐ People profiles
- ☐ Personal finance
- ☐ Regulatory changes
- ☐ Tax issues
- ☐ Women in business

**4. How did you acquire this copy of Enterprise:**

- ☐ In Business Week issue
- ☐ From Office Depot store
- ☐ From business associate, relative or friend
- ☐ Other \_\_\_\_\_

**5a. Would you like to see future issues of Enterprise?**

- ☐ Yes
- ☐ No

**5b. If yes, how many issues per year would you like to see?**

- ☐ 2
- ☐ 4
- ☐ 6
- ☐ 12

**5c. Would you pay a modest price for a subscription to Enterprise if it was published as a free-standing magazine dedicated to small business?**

- ☐ Yes
- ☐ No

**6. Please put your age in the space provided:**

\_\_\_\_\_

**7. Are you:**

- ☐ Female
- ☐ Male

**8. What is the highest level of education you have attained?**

- ☐ Some High School
- ☐ High School Graduate
- ☐ Some College (no diploma)
- ☐ College Graduate
- ☐ Some Post Graduate
- ☐ Graduate Degree

**9. Do you work primarily from your:**

- ☐ Home
- ☐ Office

**10. If you primarily work in an office, do you also do work for your job at home?**

- ☐ Yes
- ☐ No

**11. If yes, how often do you work at home for your job?**

- ☐ Often (several times each week)
- ☐ Frequently (at least once per week)
- ☐ Sometimes (two to four times/month)
- ☐ Occasionally (less than once per month)

**12. Approximately how many employees are there in your entire company?**

- ☐ 1
- ☐ 2-4
- ☐ 5-9
- ☐ 10-24
- ☐ 25-49
- ☐ 50-99
- ☐ 100-499
- ☐ 500-999
- ☐ 1,000 or more

**13. Please indicate if you have a of the equipment listed below your home or office?**

- |                                             | Home                     | Office                   |
|---------------------------------------------|--------------------------|--------------------------|
| Personal Computers (Desktop or Workstation) | <input type="checkbox"/> | <input type="checkbox"/> |
| Personal Computers (Laptop or Portable)     | <input type="checkbox"/> | <input type="checkbox"/> |
| Modem                                       | <input type="checkbox"/> | <input type="checkbox"/> |
| CD Rom Drive                                | <input type="checkbox"/> | <input type="checkbox"/> |
| Networking Hardware/Software                | <input type="checkbox"/> | <input type="checkbox"/> |
| Copiers/Duplicators                         | <input type="checkbox"/> | <input type="checkbox"/> |
| Facsimile/Fax                               | <input type="checkbox"/> | <input type="checkbox"/> |
| Typewriters                                 | <input type="checkbox"/> | <input type="checkbox"/> |
| Cellular phones                             | <input type="checkbox"/> | <input type="checkbox"/> |
| Pagers/beepers                              | <input type="checkbox"/> | <input type="checkbox"/> |
| E-mail system                               | <input type="checkbox"/> | <input type="checkbox"/> |

**14. Where do you shop for your office supplies?**

- ☐ Office Depot
- ☐ Office Max
- ☐ Staples
- ☐ WalMart
- ☐ Wholesale/Warehouse Club
- ☐ Local Stationery Store
- ☐ Other \_\_\_\_\_

Thanks for your time and thoughts. Your cooperation is very much appreciated. Please fax back this survey to 516-935-4092.

BusinessWeek

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# THE FALL OF A TIMBER BARON

y Louisiana-Pacific's board decided to dump Harry Merlo

Harry A. Merlo never thought it would end like this. Late one Friday in July, the 70-year-old chief executive of Louisiana-Pacific was summoned to a meeting of Portland (Ore.) lumber company's board. Assembled was a somber-looking collection of close friends, including test pilot Chuck Yeager and loyal business associates dating back 20 years. The meeting was brief: Directors asked Merlo and his top two lieutenants to resign immediately. "It was a complete surprise to him," says one Merlo associate present. "The company was devastated."

The boardroom coup marks a stunning reversal for Merlo. As recently as this spring, the still-vigorous CEO was basking in the glow of a seemingly flawless rise from immigrant of poor Italian immigrants to a hugely successful lumber tycoon. After 27 years at the helm, Merlo had

made over LP: By relentlessly pushing subordinates to boost production and making risky bets to develop new products, the hard-charging former Marine had built once-modest LP into a \$3 billion empire. And thanks to a new process for making wood substitutes that Merlo had pioneered, 1994 income hit a record \$347 million.

An admiring board rewarded Merlo

generously: His 1994 salary and bonus hit \$5 million, even as LP provided him with such perks as use of company jets, a 107-foot yacht to sail the Pacific, and an estate in the tony West Hills section of Portland. Over the years, Merlo also amassed 2 million shares—a 1.8% stake now worth \$48 million.

But Harry Merlo's luck was already running out. For years, there had been troubling reports that LP's wood substitute—its most profitable product—was defective when used as exterior siding. But even as warranty claims piled up, the charismatic Merlo calmed his handpicked board with promises of improved production techniques.

**STACK OF SUITS.** Far more difficult to explain away was news in April that the company was all but certain to be indicted by a federal grand jury in Colorado for environmental violations and fraud involv-



**BITTER TASTE:** Merlo feels betrayed, friends say

## When Harry Met Trouble

**1980** Louisiana-Pacific CEO Harry Merlo launches "oriented strand board," an inexpensive wood substitute. By 1985, OSB markets OSB as exterior house siding, and OSB becomes company's top-selling product.

**1990-1994** Thousands of homeowners in Florida complain that OSB siding deteriorates in the humid climate. Three class-action lawsuits are filed. One has been settled; the others are pending.

**1991-92** Minnesota Attorney General sues LP over defective siding. Company settles, agrees to pay for repairs. By yearend, LP has paid \$22 million to settle OSB claims nationwide.

**AUGUST, 1993** An ex-employee sues Merlo, alleging sexual harassment. Merlo and the company refuse to comment, and the suit is pending.

**MAY-SEPTEMBER, 1995** With 12 class actions alleging defective OSB siding, LP's liability could hit \$300 million. As litigation mounts, LP's board launches internal investigation.

**JUNE, 1995** Colorado grand jury indicts LP and two plant managers for environmental violations and fraud involving OSB. With OSB now accounting for 25% of LP's \$3 billion sales, the stock tumbles to 22 from all-time high of 44 in 1994.

**JULY 3** LP's board announces Merlo's ouster and begins search for replacement.

DATA: COMPANY REPORTS, BUSINESS WEEK



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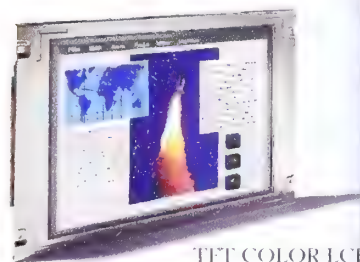
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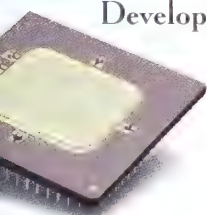
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ing its manufacturing processes. That has sparked a dozen shareholder lawsuits. At the same time, the stack of homeowner lawsuits alleging flawed siding was growing fatter, while a 1993 lawsuit charging Merlo with sexual harassment had never been resolved.

Meanwhile, increasingly antsy shareholders had sent LP's shares tumbling from an all-time high of 44 in early 1994 to 22 last spring (chart, page 92). Finally, David E. Nelson, a principal with Investment Counselors of Maryland Inc. and one of LP's biggest shareholders, sent Merlo a letter requesting a meeting.

of the University of Virginia's business school. An environmental specialist invited onto the board by Merlo in 1993, Guiton Hill is the only board newcomer, and she spearheaded the investigation.

Trouble first came in 1990, when scores of homeowners in humid Florida began complaining that LP's siding quickly became waterlogged and deteriorated in the rain. Thousands of individual claims were eventually consolidated into three class actions. LP has now settled one suit—agreeing to pay for repairs that could total \$30 million—while the other two are pending. Although LP no

of revenues and roughly 35% of profit.

At first, builders used strand board only for floor and roof sheathing. For such applications, it has performed well and been widely copied. But Merlo overreached in 1985 when he decided to market a version of OSB as siding in place of the usual cedar. Just a few years after installation, the material began to deteriorate, according to thousands of class actions and state and federal investigations. Unable to withstand humidity, the siding boards have rotted and cracked. In moist climates, houses have sprouted mushrooms and other



**SOMETHING ROTTEN:** Homeowner Steven Eklund is disgusted with his moldy siding

But Nelson says Merlo never responded to the letter or to repeated phone calls. Nelson began to draft a letter to the board, but never had a chance to send it. With questions piling up, the board had hastily launched an internal probe. The result: Six weeks after the Colorado indictment came on June 15, Merlo was out of a job, along with his two top aides, James Eisses and Ronald L. Paul. **"WEED" TREES.** Merlo declined to speak with *BUSINESS WEEK*. But friends say he is bitter and feels betrayed. Merlo "lived and breathed" Louisiana-Pacific, says Portland businessman and longtime associate Gerry Pratt. "He still talks about 'my company.'" The interim CEO, longtime board member and former LP Chief Financial Officer Donald R. Kayser, says the move was wrenching yet unavoidable. Others are harsher. "Exposing the company to such losses and litigation is just inexcusable," says director Bonnie Guiton Hill, who is dean

longer sells siding in Florida, problems were only beginning. The company quietly settled similar charges with the Minnesota Attorney General, while another 10 class actions around the country remain unresolved.

Ironically, Merlo's problems stem from a product that had been his biggest triumph—a cheap plywood substitute known as oriented strand board (OSB). Merlo had vigorously championed OSB, which is made from paper-thin slices of small trees that are glued together with resin, starting in 1980. While other forest-products companies worried about the diminishing supply of big trees from which plywood was cut, Merlo bet that by using "weed" trees that others spurned, LP could create a substitute. The risky move paid off, and OSB became hugely popular. The product, which comes with a 25-year warranty, fueled LP's bottom line for the last decade. By 1994, OSB accounted for 25%

**"Exposing the company to such losses and litigation is just inexcusable," says director Bonnie Guiton Hill**

fungi. "I can poke my finger through it," says Portland homeowner Steven Eklund. "It's a real mess."

Kayser denies that the siding is flawed, and LP continues to sell it in most states. He says the company will "aggressively fight"

growing litigation while striving to improve quality. "If there is a problem we'll fix it," he says. "We never claim to have zero defects."

Still, as the problems were mounting, directors grew increasingly anxious over rising payments for defective products: \$5 million in 1993, \$10 million in 1994, and \$7 million in this year's first half. After years of denial, when Merlo finally admitted that the litigation would hit LP financially this spring, investor support dried up. "All of a sudden, what had not been a material problem became one," says Nelson.

Yet even the news in April of the pending indictment alleging problems at the company's Montrose (Colo.) plant didn't appear to worry Merlo. With typical bravado, he offered to resign. The eight-member board—which, besides Merlo, included three current or former company executives and Merlo's hunting buddy Yeager—insisted he stay. "We

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# UNISYS





## Kayser says his predecessor's racy lifestyle wasn't a factor in his ouster. But the company jets and yacht are for sale

refused, and he knew we would," says one director.

But with Guiton Hill increasingly pushing the board to act—and directors' growing fears that they would be liable—that soon changed. With Merlo's consent, the board hired San Francisco law firm LeBoeuf, Lamb, Greene & MacRae to prepare a report on the alleged problems at Montrose. But Guiton Hill also chaired an outside board committee that authorized investigating attorney Charles B. Renfrew to conduct a more far-reaching probe. "The days of rubber-stamping are over," Guiton Hill says. "When problems reach the breaking point, you have to take action."

**AUTOCRATIC STYLE.** When the grand jury indictment finally came on June 15, the pressure on Merlo mounted. The 56-count charge suggests a company rife with environmental violations and sorely lacking in quality-control measures. The indictment alleges that plant managers and employees at the Montrose plant tampered with pollution-monitoring devices, at times turning them off completely. The grand jury also charged that Louisiana-Pacific routinely cut corners in manufacturing: It allegedly sold low-grade strand board to contractors, then fraudulently substituted higher-quality samples when industry auditors came to certify the boards were of the quality required for home construction.

LP has pled not guilty to the allegations. Renfrew, a retired federal judge and former federal prosecutor, won't comment on what his investigation turned

up. Interim CEO Kayser declines comment, except to say, "We are vigorously defending ourselves." And he insists there is "no linkage" between the charges and Merlo's ouster. Instead, he says, Merlo was ousted because Renfrew's confidential findings revealed "serious problems with management practices and style."

Those findings centered on what company sources say was the increasing damage caused by Merlo's aggressive, autocratic style. Despite the company's rapid growth, former executives describe an entrepreneurial manager

who, together with his two top lieutenants, continued to make all key decisions. Merlo pushed relentlessly for ever higher productivity and ever lower costs—and instilled a demanding, performance driven culture. At one Texas plywood plant, for example, a sign on the wall read: "Work, or get your ass kicked." Although success was well-compensated, promotions were rare. "Merlo hates titles and organizational charts," says one former top exec. "He ran Louisiana-Pacific as if it were a small startup." That may have been a virtue early on, but Merlo's refusal to build stronger middle management led to poor controls—especially worrisome when coupled with pressure for better numbers. Says Guiton Hill: "Management was very, very, very thin."

Others defend Merlo as a gifted if abrasive visionary whose downfall was sped by his flamboyant manner. Pratt and others say Merlo had long rankled the insular Portland business community by avoiding the country club set. Says Pratt: "They didn't like his style."

Instead, the perennial bachelor raised eyebrows with his opulent lifestyle: He threw lavish parties at his \$900,000 company-owned estate or on the

yacht, using LP's private jets to fly celebrity guests such as tenor Lucia Pavarotti. And friends acknowledge that Merlo was known for hiring stunning women as his assistants; even today, "never goes anywhere without a tall, attractive blonde on his arm," says Poland businessman Edward Pietz. That led to further trouble: In mid-1993, ex-assistant to LP's CFO filed suit against Merlo for sexual harassment, alleging the company hired top assistants only if they were "young, strikingly attractive and likely to acquiesce to sexual advances by the CEO." Merlo and the company refuse to comment on the allegation, and the suit is pending.

Kayser says Merlo's lifestyle never interfered with work, and he denies that the harassment charges were a factor in his ouster. Still, within a month of Merlo's leaving, the company planes and yacht went on sale as "underutilized."

Kayser is left with the unenviable task of setting LP back on track. The company recently restated its second quarter earnings, reducing them by \$10 million, to \$26.3 million, to build reserves for growing claims and legal expenses. "Our priority is to bring all litigation to an early closure," he says. Analysts estimate the company's liabilities could reach \$300 million or more.

In the meantime, Kayser has broken LP into smaller units, added extra management, and hired a head of compliance. He hopes to name a new CEO in January. As for Harry Merlo, he has remained mum. Supporters say that, with extensive other interests, including

stakes in a local semiconductor manufacturer and a software house, he will remain a player in the Portland business scene. And, some locals speculate, he may try to seize back control of "his" company with hostile tender offers. Just in case Kayser and his newly vigilant board didn't have enough worries.

By Eric Schin  
with Anita Marks,  
Portland

### LP'S STOCK CRUMBLES





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MARKETS

# WHY THE BULL STILL HAS RUNNING ROOM

ate of bad earnings reports won't hurt much

at least three weeks before Corporate America starts swamping the newswires with quarterly earnings reports, but already there's a growing sense of uneasiness in the air. On Sept. 13, IBM, the stock market's comeback kid, told Wall Street analysts that its third-quarter profit forecasts were too high. During the following days, other high-profile technology companies such as Apple Computer Inc. and Oracle Corp. also deflated expectations. It's not just technology. Caterpillar Inc., an old-line industrial giant, turned tough world-class competitor on Sept. 19 that earnings would fall below year-ago levels.

The four stocks went pffft, though the market has since recovered somewhat. But then, the unexpected bulletins dealt a little kidney punch to the ragged bull market. After inching above 4800 on Sept. 14, the Dow industrial average declined for three days, but came roaring back to close at 4793 on Sept. 20. **BLE DIGITS.** For now, the market's going to blow off some bad earnings reports. Cash continues to pour into mutual funds at a torrid pace, and the stronger dollar is luring foreign investors to the U.S. market for the first time in years. Wall Street analysts, however, still are forecasting hefty dou-

ble-digit profit gains for the third quarter vs. the same period of 1994. Says Charles G. Crane, director of research at money-manager Spears, Benzak, Solomon & Farrell: "We're not expecting any dramatic earnings disappointment during this period."

Indeed, nearly all the major market indexes continue to trade near or at all-time highs. And despite some troubles in tech-land, the Pacific Stock Exchange Technology Index is also at a high. But moving the averages much higher won't be so easy. Profits, one of the driving forces in this bull market, are losing some of their powerful momentum.

Corporate America as a whole has beaten Wall Street analysts' earnings forecasts for the last nine quarters in a row. Now, Benjamin L. Zacks of Zacks Investment Research thinks companies on average will meet an-

alysts' third-quarter forecast of 17.5% profit growth, "but fewer companies will beat the expectations, and those that beat them will do so by slimmer margins." The bottom line on bottom lines: Earnings will rise again, but at a slower rate.

**"INFLECTION POINT."** While not a sell signal per se, the deceleration is a reminder of the advanced age of the bull market and the economic expansion upon which it is built. "We're at the inflection point going from a period of very powerful earnings momentum to a lot trickier period of earnings gains," says Richard B. Hoey, portfolio manager of the Dreyfus Growth & Income Fund. "Profits are already at a high level, the economy is past the period of strong growth, and it's going to be difficult to show big earnings growth from here on out."

That's part of the problem with Caterpillar, which must cut back production because of slowing sales and higher inventories. Other companies are being hurt by the strengthening dollar, whose weakness long bolstered profits by making U.S. exports cheaper and by boosting earnings of overseas subsidiaries when translated back into dollars. On Sept. 19, Polaroid Corp. revised its profit forecast downward, in part because the rising dollar cut the value of its overseas profits.

Even if third-quarter profits pale a bit, though, the stock market is not in any great danger. Inflation is tepid and long-term rates are down—and could head lower. The market remains supremely liquid, and many investors have not given up hope for another cut in short-term rates from the Fed—if not at the Sept. 26 meeting, then at the next one. That would keep stock prices aloft.

Even at current rates, stocks are not overpriced. Stanley Levine, quantitative research director for First Call Corp., figures stocks are still about 11% undervalued based on earnings estimates and interest rates. There's still plenty of margin before stocks become more expensive than bonds, even if the market takes a few more kidney punches.

By Jeffrey M. Laderman in New York

## UNWELCOME SURPRISES

How September news moved big stocks

|                                                                              | BEFORE NEWS | SEPT. 20 |
|------------------------------------------------------------------------------|-------------|----------|
| <b>CATERPILLAR</b>                                                           | 65%         | 59%      |
| Cutting output; third-quarter profits will fall below last year's            |             |          |
| <b>ORACLE</b>                                                                | 44%         | 39%      |
| Revenue gains of 39% weaker than forecast, indicating slower growth          |             |          |
| <b>APPLE</b>                                                                 | 40          | 36%      |
| Production problems, slimmer margins will push earnings well below estimates |             |          |
| <b>IBM</b>                                                                   | 97%         | 95%      |
| Delay in shipping new mainframes will lower third-quarter earnings           |             |          |

DATA: BLOOMBERG FINANCIAL MARKETS



# THE SHOWDOWN IN GLOBAL BANKING

Europe's giants are set for a slugfest with their U.S. cousins, and the stakes are huge



The sound of jackhammers and backhoes intrudes on the daily rituals of the London office of Morgan Grenfell Group PLC, where a gaping hole in the ground outside is hastily being transformed into a new headquarters. But the noise doesn't faze the staff inside. A dozen visitors with bulging briefcases parade through the revolving door in the space of 10 minutes. They are whisked off to private chambers by women in white blouses and gray skirts, who later bring them tea on lacquered trays. The smell of dealmaking permeates the air.

These are heady days for the 152-year-old London merchant bank. After watching American securities firms steal their clients for the past five years, Morgan Grenfell is hitting back. Germany's Deutsche Bank just moved its Frankfurt-based investment banking unit to London to merge with Morgan

**“The combat zone is the international issuer.... We're not looking to go head-to-head with Wall Street”**

— DAVID BAND, BZW

Grenfell, which Deutsche acquired in 1989. Now, the combined Deutsche Morgan Grenfell (DMG) is adding staff all over the globe, even raiding entire teams of specialists from Merrill Lynch & Co. and other rivals.

DMG is building trading floors the size of football fields in New York and London. And it's competing aggressively for business against Merrill Lynch, Goldman Sachs, and Morgan Stanley,

the industry leaders. In a few years, DMG hopes to claim what it believes is its rightful spot as one of the five biggest investment banks in the world, and certainly the biggest in Europe. “I'm afraid the U.S. banks are going to have to get used to seeing Deutsche Morgan Grenfell more often,” says Chief Executive Michael W.R. Dobson.

Hubris? Perhaps. But Dobson isn't the only one puffing up his chest these days. Europe's giants of high finance are readying themselves for a slugfest against the titans of Wall Street. The Eurofighters are a dozen deep-pocketed Swiss, British, Dutch, French and German universal banks, some that do commercial as well as investment banking. And they have embarked on a do-or-die campaign to beat out rivals, build distribution networks in the U.S., and open new offices in emerging markets around the world. Like DMG, all want a place in the top tier. “There's a determination among European banks to succeed, whatever the cost,” says Luqman A. Nold, head of global capital markets at France's Banque Paribas.

**ELITE CIRCLE.** If their strategies work, European banks may win back some of the financial

clout and prestige they have given up to Wall Street since the 1980s. But the losers in this high-stakes game could suddenly find themselves in the same position as S.G. Warburg Group PLC, once Britain's most prestigious investment bank. It was subsumed by the far-larger Swiss Bank Corp. the year after an aggressive expansion in the U.S. weakened its financial position and left it unable to recover from





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an aborted attempt to merge with Morgan Stanley & Co.

In going global, the Euros are up against formidable competition from the other side of the Atlantic. U.S. investment banks own 70% of the market for all debt and equity underwriting worldwide, acquired largely by managing debt and equity issues for U.S. corporations. European houses, reluctant to commit big bucks to dealmaking, were unable to penetrate this elite circle in past years. With little competition, the U.S. banks could command high fees for handling initial public offerings or big mergers.

The fees subsidized their overseas development at the Europeans' expense. But changes in the structure of the global securities market are every bit as important. Wall Street's oligopoly is breaking up, with large commercial banks moving into investment banks' territory. U.S. issuers want to reach a global investor base, and the appetite for international securities has grown enormously outside the U.S., as well as within. In these changes, the Europeans contend, lies opportunity.

**NEW WAVE.** Take BZW Ltd., the investment banking arm of Britain's Barclays Bank PLC. Since losing a bundle trying to sell stocks in New York in 1990, BZW has regrouped. It now has 1,500 people in New York trading currencies and derivatives and selling foreign securities to U.S. institutions. It's also making money worldwide, recording \$200 million in operating profits in the first half of 1995. "The combat zone is the international issuer and the international investor," says CEO David Band. "We're not looking to go head-to-head with Wall Street."

Well, not on Wall Street's home turf, at least. What Band and other European investment bankers are aiming to catch is the new wave of globe-spanning deals now beginning to build. Over the next five years, the biggest issuers of debt and equity won't be Americans with inbred ties to Wall Street. They will be Eastern and Western European governments privatizing companies, or Asian and Latin American governments building power plants, dams, and roads. A

\$30 billion flood of telecom privatizations is due out in the next year alone, and the World Bank estimates that East Asia will need \$1.5 trillion for infrastructure over the coming decade.

And who will invest in such ventures? U.S. pension and mutual funds will remain heavily involved, and Europe's securities houses will be pursuing them alongside their Wall Street rivals. But a new, global investor base also is

nies with growing U.S. operations and another market the Euros don't want to lose. When German conglomerate Daimler Benz listed its shares on the New York Stock Exchange in 1993, Deutsche Bank and Goldman, Sachs & Co. led the deal. But the Europeans have U.S. corporations in their sights as well. U.S. companies are increasingly tapping global capital markets to sell stocks and bonds and finance everything from manufacturing plants to sales offices overseas.

The Europeans are going after their business. "We get pitches constantly," says AT&T Treasurer Larry Prendergast, who has used the Union Bank of Switzerland, Swiss Bank, and Deutsche Bank as lead dollar-denominated bond deals in Europe. Monsanto Co. Treasurer Juanita H. Hinshaw, meanwhile, included UBS as part of a recent bond syndicate, the first time the chemical company chose an overseas bank to market its debt. "We were happy with their aggressive selling capabilities," says Hinshaw. "We had confidence they could sell our bonds."

**UPSETS.** While the U.S. battle is just beginning, the Europeans are scoring some notable wins in emerging markets. In Sept. 12, the World Bank chose Deutsche over Morgan Stanley to raise \$1.25 billion for a hydroelectric power project serving South Africa and Lesotho. The decision came only two months after the World Bank allowed Deutsche—along with Lehman Brothers Inc.—to lead-manage the sale of \$1.5 billion worth of dollar-denominated bonds.

Swiss banks have also been aggressive. UBS bested Goldman Sachs in last year's \$800 million convertible-bond deal for Formosa Plastics Corp., a Taiwanese company that UBS previously served as a lender. UBS won the deal, a top executive claims, because his institution isn't "a suitcase investment bank," his term for the Wall

Streeters who invade a country to make a pitch and then depart. And the Europeans have enjoyed a measure of success. In July, BZW beat out Lehman Brothers, Salomon Brothers, and J.P. Morgan to take the much-coveted lead role in the \$1 billion privatization of Italian telecom group STET. BZW also was chosen to advise the Australian government in

## How Europe Is Moving Into Investment Banking



### Taking Over Competitors

Germany's Dresdner Bank acquired Britain's Kleinwort Benson for \$1.5 billion. Rival Deutsche Bank consolidated global investment banking in London under the Deutsche Morgan Grenfell flag. Swiss Bank Corp. bought Britain's S.G. Warburg and 25% of Perot Systems, while Holland's ING took over Baring Securities.

### Capturing Deals

Barclays de Zoete Wedd will run the \$7 billion sale of Italy's state phone company, STET. Swiss Bank handled a \$100 million financing for Mexican cement maker Apasco. And Union Bank of Switzerland won a \$600 million bond issue for Formosa Plastics.

### Seeking New Talent

Deutsche Morgan Grenfell ponied up big bucks to sign up Edson Mitchell, co-head of Merrill Lynch's fixed-income group. Barclays de Zoete Wedd hired Mark Seligman, former head of Warburg's merger advisory team, as co-head of corporate finance.

forming, and it's entirely up for grabs. All across Asia, middle-class savers are getting into mutual funds. And European and Latin American governments and companies are forming pension funds to supplant state retirement systems. All should become markets for international securities—just what the Europeans love to peddle.

The thousands of European compa-





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effort to bring 22 airports to the stock market, and it is managing the flotation of Indonesian tin-mining company Tambang Timah. "They've made headway in Europe and to a lesser degree, Asia," Merrill Lynch Executive Vice-President Jerome P. Kenney says of his newly invigorated European competition. "They clearly have gained."

Still, the challenge for the Euros will be to combine the best of the Old World's client-focused style with the

rill is considering further acquisitions in Europe, possibly a fund management group or brokerages in France and Spain.

Of course, Merrill isn't the only Wall Street house intent on maintaining its market share abroad. Goldman Sachs, for one, is sharing the global coordinator role with DMG on what's likely to be the biggest equity flotation in history, next year's \$10 billion Deutsche Telekom privatization. Goldman is one of

com deals, the Americans also surpass the Europeans in distribution of new securities.

Overcoming this handicap will take time and money. Still, if the pace of privatizations and IPOs continues to pick up, there should be plenty of spoils go around. And the fat fees that come with the coveted "global coordinator" role in global securities sales explain why the Euros are so eager to chase deals—especially equity IPOs. Underwriting syndicates are paid 3% of a worldwide issue's face value to cover the costs of managing an equity deal. But the global coordinator keeps half—or more—of the take.

**ELUSIVE GOAL.** As Wall Street and Europe slug it out, however, the payoff is declining. In some cases, bidders are discounting to win new business or get a foot in the door of a syndicate. The prospect of slimmer profit margins on their lucrative overseas business irks Wall Streeters, who already are angered at the Euros' use of million-dollar bonuses to lure away some of their best performers. "Given the practically unlimited amount of capital the European banks have, they can buy people, buy firms, and create a lot of disruption with clients," says Peter Davis, a Booz, Allen & Hamilton Inc. partner. "The [Wall Street] view is, it will screw up a good thing."

In fact, John Leonard, a London-based analyst with Salomon Brothers Inc., thinks that globalization will prove an elusive goal for many new players. "When everybody does it," he says, "it's usually a bad sign, that money's being wasted."

Even some top Euro bankers concede that only a few players will be able to assemble the right mix of capital, technology, and distribution to do alongside Wall Street's heavies. But to tell the folks at any European investment bank that some will fall behind. "You're going to see increased fierce competition," says Marcel Ospelt, the Swiss Bank investment banker who led the takeover of Warburg. Out of this competition could come the financial realignment in international investment banking since Wall Street went global a decade ago. A lot of tears will be shed along the way.

*By Paula Dwyer in London, and Bill Javetski in Paris, Leah Nathanspiro in New York, Pete Engardio in Hong Kong, and Geri Smith in Mexico City*



**PHONE BOOM:** The Europeans see enormous chances in telecom privatizations

New World's emphasis on transactions. On both sides of the Atlantic, J.P. Morgan & Co. is considered a model. Morgan is one of the few U.S. commercial lenders to move successfully into investment banking. The Mexican government is showing its gratitude to Morgan for not turning tail during the peso panic. The reward: Morgan gets to help Mexico restructure its debt. It will also be exclusive agent in the sale of Pemex' petrochemical units in October. "They're not the kind of bank that does one deal, collects its fees, and is gone. They stay with you," says Ricardo Sada, who is treasurer of Hylsamex, a steel-producing subsidiary of the Monterrey-based Alfa conglomerate.

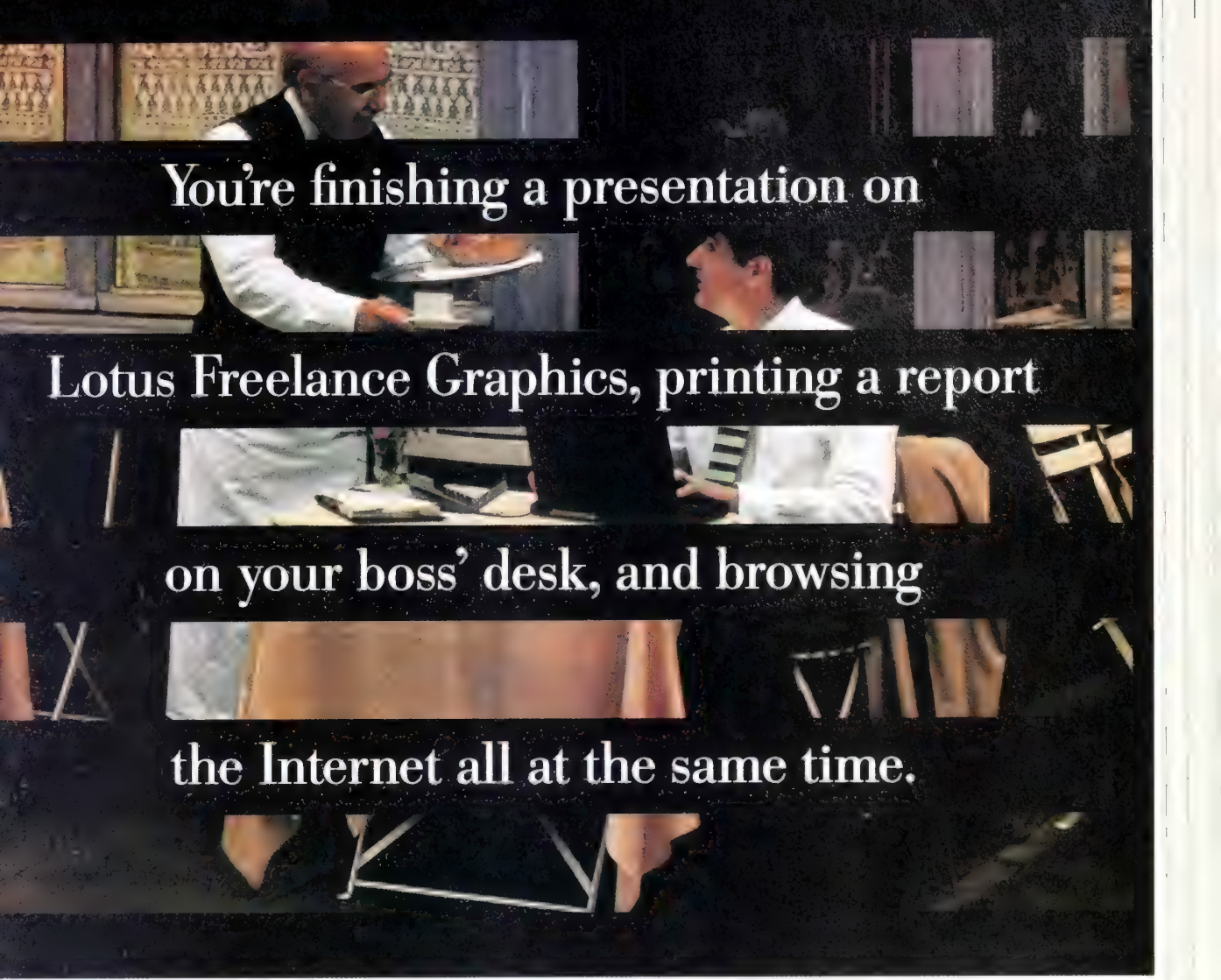
**DEEPER ROOTS.** Indeed, Merrill Lynch recognized the growing importance of having a permanent local presence rather than just a handful of people available to parachute into a country. In July, it paid \$810 million for Smith New Court Securities Ltd. In addition to being Britain's largest equity brokerage and research house, SNC has developed deep roots in the emerging markets of Russia and Eastern Europe. Now, Mer-

four lead bankers on Indonesia's \$3 billion PT Telekom privatization later this year and advised the Dutch on privatizing KPN, the state telecom company.

Indeed, despite the Euros' early victories, the transatlantic battle for market share is likely to be long and bloody. A senior official at Bezeq Telecom, the soon-to-be-privatized Israeli telephone company, says that all the major U.S. and European banks bid for the lead role in handling the partial sale of the government's stake early next year. "But it was clear from the start we would be going with an American bank." Why? In addition to their deep knowledge of the Israeli market and their global skills handling tele-

**"When everybody does it, it's usually a sign money's being wasted"**





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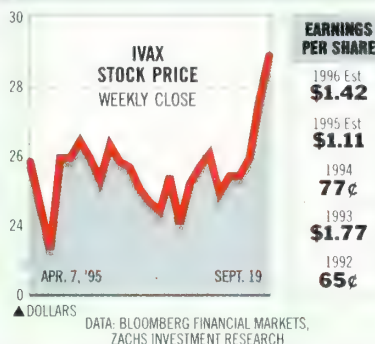
BY GENE G. MARCIAL

## COULD IVAX GET SWALLOWED?

Short-sellers on the run. Insider buying heating up. And takeover whispers getting louder. All that action is fueling a resurgence in the stock of IVAX (IVX), the nation's largest generic drugmaker, making the shares leap from 24 to 29 in recent weeks. What's going on?

The shorts are still very much on IVAX' back, but they have taken a beating as the stock has jumped. IVAX has been talked about as a takeover target all year, but it now is starting to appear

### FEELING BETTER ALREADY



much closer to doing an actual merger deal, says one investment banker.

Analysts estimate the drugmaker's value at 40 a share on fundamentals alone, based on the company's projected 1996 earnings. (In 1994, the stock's price climbed as high as 38.) One analyst, whose investment firm has banking ties with IVAX, figured that the drugmaker's earnings in the fourth quarter of 1996 could approach \$2 a share on an annual basis. So IVAX is a shoe-in to hit the 40s next year. In the pharmaceutical industry, the average p-e is 22, vs. IVAX's current p-e of 20.

In spite of the stock's 30% climb this year, some corporate insiders, including Chairman and CEO Philip Frost, have stepped up their buying. In August, Frost exercised options for 1.4 million shares, which set him back more than \$1 million. That move boosted his stake to 15%.

Takeover speculation has been driven by a recent purchase by BASF, a large German drug-and-chemical conglomerate, by which it acquired a 4.9% stake in IVAX. Some investors argue

that the buy was just an initial step toward building up a major position in IVAX. BASF may be forced to accelerate its buying because of the advance in the stock's price. In March, IVAX and BASF formed a joint venture to set up a generic-drug operation in Germany. "That will eventually expand, we expect, to the rest of Continental Europe," says analyst David Saks of Gruntal & Co. "BASF may take a larger equity position, with an eye toward a merger."

BASF may not be the only suitor, however, says one investment banker. "There are other pharmaceutical companies in Europe and the U.S. who I would say are suitors," he insists. One such, he adds, is Bayer, another German giant. "IVAX has positioned itself in the generic and nongeneric drug business in such a way that it makes a good fit with many European drug companies," says one IVAX insider. Frost declined comment.

## O COME YE TO BETHLEHEM

Everyone is looking for the ignored, undervalued stock. But it takes guts to plunk down money on a stock that's down and out of favor. Investment pro Larry Rice makes a fine living doing just that: With gusto, he goes after unwanted stocks—those he thinks will be the next darlings of the mutual funds. One such stock he likes: Bethlehem Steel (BS).

Rice is snapping up shares even though Wall Street types are nearly unanimously bored with the steel industry. "Bethlehem doesn't make memory chips or new drugs—there's no sex to the Bethlehem story," he says. But Rice, chief investment officer and director of research at Josephthal Lyon & Ross, is bullish nonetheless.

Why? He thinks the stock, which has been meandering around the mid-teens, will hit the 20s in 6 or 12 months. It's trading at 14 a share—not far from its 52-week low of 13%. But, says Rice, Bethlehem "has downsized, upgraded its mills, and become very competitive with steel producers here and abroad."

He expects the mutual funds will go after steel stocks when they realize that the world economic outlook is brightening. Contrary to popular belief, Rice adds, demand for steel will firm up along with prices. Zachs In-

vestment Research sees Bethlehem making \$2.58 a share in 1996 and \$1.77 this year, vs. 1994's 35¢.

## TOP SOURCE GETS TUNED IN

Overhead radio speakers and oil analyzers: They don't sound like stunning breakthroughs. But they are—at least for Top Source Technologies (TPS), whose shares have spurted from 5½ to 7¼ in four months. Three years ago the stock was at 2¼.

Top Source's overhead speakers are a success in Chrysler's Grand Cherokee and Jeep Wrangler. In addition, Top Source has filed a patent for a front overhead-mounted system with shock absorbing materials. This would eliminate the need for speakers on the dashboard and doors.

The company's on-site oil analyzer provides refineries, chemical plants, or vehicle-fleet operators a scientific breakdown of a sample from an engine or transmission. The analysis measures contaminants, such as metal debris, coolant, and unburned fuel. "Our analyzer helps clients to improve fuel economy and reduce exhaust emissions," says Chairman Stuart Landow. "Interest in the analyzer among refiners has been strong."

So far, two multinational oil companies have leased the analyzers, for which they pay a fee of \$10 per test. But Landow would not identify the companies.

One pro says analysts will go this month to two other clients: an oil company, said to be Texaco, and a dealer for Cummins Engine.

"These new orders confirm the efficacy of the analyzers as well as the potential demand for them," he says.

Revenues are flowing from the speakers. This year, the oil analyzer is expected to kick in, too. After years in the red, Top Source will report a profit in the year ending Sept 30, 1996, says Jonathan Garriss of Hampshire Securities. He sees earnings of 11¢ a share in fiscal 1996 and 56¢ in 1997, vs. an 8¢ loss this year.

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## JPMorgan



# Informed Consent

BY JOHN A. BYRNE



The controversy surrounding silicone breast implants has plunged Dow Corning Corp. into bankruptcy. More than 8,000 women still have lawsuits pending against the company, which has spent \$1 billion defending itself. On Sept. 13, a federal judge ruled that suits against parent companies Dow Chemical Co. and Corning Inc. could proceed despite the bankruptcy filing. All this because of a product that produced less than 1% of Dow Corning's revenues.

John E. Swanson viewed this debacle from a unique vantage. For most of his 27 years at Dow Corning, he shaped its ethics program, which was

acclaimed as a model for Corporate America. His wife, Colleen, had Dow Corning breast implants. After years of devastating illnesses, she became convinced that her implants were destroying her health—and that the company had failed to inform women of the risks. In time, John came to agree. He also came to believe that his company had acted unethically through much of the crisis.

The circumstances John Swanson faced were remarkable. But his experience is emblematic of the ethical conflicts any executive can face. What happens when personal values clash with corporate beliefs? What happens when a moral choice separates you from your company's official position and from your colleagues in a close-knit organization? Here, in an adaptation from a forthcoming book by Senior Writer John A. Byrne, is the harrowing tale of how one manager faced those questions.

FOUR WEEKS EARLIER, COLLEEN SWANSON HAD BEEN OUT COLD ON AN OPERATING TABLE AT CLEVELAND'S MOUNT SINAI MEDICAL CENTER. A surgeon had worked three hours to remove the silicone breast implants that had been in her chest for 17 years—and that Colleen was sure were the cause of health problems that had for years eroded her

Since the grueling operation, she had been bandaged from collarbone to waist. Now, on a bright and beautiful morning in July of 1991, she would get the first glimpse of how she looked. Her husband, John, had already left for his job at Dow Corning—the maker of the implants.

Once, John had loved his job and his life in little Midland, Mich. But for years, he had shared Colleen's anguish, com-

*From Informed Consent: A Story of Personal Tragedy and Corporate Betrayal...Inside the Silicone Breast Implant Crisis by John A. Byrne. Copyright © 1996 By John A. Byrne. Reprinted by permission of The McGraw-Hill Companies*



### **MOMENT OF TRUTH**

*She climbed out of bed and walked to the bathroom, consciously avoiding the full-length mirror on the bedroom wall, and went to the smaller mirror over the sink. Before flicking on the light, she closed her eyes once more and tensed. Finally, she stared at her reflection.*



ing her through ailments including severe migraines, debilitating joint pain, and extreme fatigue. And when he, like Colleen, concluded that her implants were the cause, he supported her decision to have them removed. Still, Colleen had purposely failed to remind him that today was the day to take off the bandages. "I

## Cover Story

really felt I wanted to deal with it myself," she recalls.

Ever since her surgery, she had tried to imagine how she would look. A petite woman of 55, Colleen was always impeccably turned out, her quietly tasteful clothes reflecting her conservative Midwestern background. She had sought the implants only to bring her small, uneven breasts closer to average. Now she wondered: Would she despise her appearance? Would John? "I knew it was going to be bad," she says, "because my surgeon had told me that most of my breast tissue had been destroyed."

She spent hours that morning summoning her courage. At last, she eased herself into a warm bath and gently splashed water over the bandages in hopes the water would penetrate the plastic tape and lessen the pain of its removal. But the bath failed to loosen the dressing, and for a time she gave up.

That afternoon, she tried again. Alone in her bedroom, she lowered the shades and lay on the bed. She began to pull at the tape, gritting her teeth against the pain. Only when the bandages were tossed aside did she glance down. What she saw made her cry out, then shut her eyes, not wanting to see any more.

She climbed out of bed and walked to the bathroom, consciously avoiding the full-length mirror on the bedroom wall, and went to the smaller mirror over the sink. Before flicking on the light, she closed her eyes once more and tensed. Finally, she stared at her reflection.

Thick, red, six-inch scars curved across each side of her chest where the creases beneath her breasts had been. Instead of breasts, there were just ridges of folded, discolored skin—like deflated balloons that had held air a long time. The left side of her chest, where more silicone had apparently leaked into her body, was nearly concave.

Colleen stared at herself for four or five minutes. She didn't recognize the frightened and pitiful woman whose trembling body was forever disfigured. Finally, she stepped into the shower and let the water wash the dried blood from the wounds. She tried to calm herself and relax, but she couldn't hold back the sobbing. "I cried and cried and cried," she recalls. "I cried for a long time."



SEVEN MONTHS EARLIER—IN LATE DECEMBER, 1990—John Swanson had opened an interoffice envelope marked "For Addressee Only" to find a shocking memo. Two company officials, it alleged, were trying to destroy internal reports that showed far higher complication rates for silicone breast implants than Dow Corning had ever acknowledged. These were serious allegations under any circumstances, but for Swanson, they had great personal significance. The memo

came from the company's medical director, Dr. Charles Dillon, who was asking the Business Conduct Committee which Swanson served to investigate "a violation of corporate professional, and commonly accepted business ethics."

Dillon's account said that Greg Thiess, a senior litigation attorney, had approached Mary Ann Woodbury, a research scientist, and asked her to destroy all copies of a memo in which she had analyzed implant complication rates. Disturbed, Woodbury had asked Dillon to join her and Thiess, and the attorney had repeated his request. "Greg stated to us that he was acting at the specific request of Robert Rylee II, vice-president and general manager of the health-care business," Dillon wrote, adding: "He also stated that the information contained in the memos would compromise projects that he was then working on in Dow Corning product-liability litigation and be adverse to the company if publicly revealed..."

Every night, John and Colleen had been debating whether she should have her implants removed. Both had begun to wonder if Dow Corning had failed to inform patients of known risks. Dillon's memo was a part of the puzzle—but it didn't reveal the complication rate Woodbury was reporting.

The Business Conduct Committee scheduled a Jan. 3 meeting to air the incident. Eager to learn more, Swanson phoned Woodbury that morning. "Can you give me just a brushstroke idea of what it is we're talking about that Bob Rylee is so concerned about?" he asked.

Woodbury said she had studied complaint data from company files and other sources, including the government. She concluded that the complaints received by the company were probably but a portion of the actual number because "it's only those that get back to us through the doctor's office." Many problems went unreported. Woodbury also believed the company overestimated the number of implant recipients, which would lower the complication rate. In the sample she studied, Woodbury had found 30.3% of women with implants experienced problems, and 13% had

the implants replaced within five years.

As it turned out, the Business Conduct Committee meeting was postponed several days. Swanson prepared the agenda, but Richard A. Hazleton, then general manager of the industrial products group, asked him not to attend. Swanson suspected it was because he seemed sympathetic to Dillon. Though taken aback, he didn't argue—perhaps because he knew he was beginning to be conflicted about implants.

So his knowledge of the session came from a summary prepared by other members of the conduct committee. The document confirmed that Thiess had been following Rylee's lead. It said: "Bob Rylee indicated that when he received the information..., he was very concerned that the way it was stated was prejudicial to Dow Corning's interests and could have adverse impact in future litigation situations. He stated he did not intend in this case, nor does he advocate in general, suppressing either factual information or professional conclusions or opinions." But Rylee wanted documentation that made clear "the distinctions between facts, conclusions, opinions of people inside and outside Dow Corning which Dow Corning agrees, and conclusions or opinions which Dow Corning does not agree."

Since 1963, when Dow Corning introduced breast implants, there had been mounting complaints that the devices ruptured far more frequently than expected.



## WHAT THE MEMO REVEALED

*Two Dow Corning officials, it alleged, were trying to destroy internal reports that showed far higher complication rates for silicone breast implants than the company had ever acknowledged. These were serious allegations under any circumstances, but for Swanson, they had great personal significance.*

The incident, the memo added, would serve as a springboard to develop guidelines for resolving future conflicts. Swanson was bitterly disappointed that his colleagues had sidestepped the larger issue: Was the company deliberately understating complication rates?

Dillon was also unhappy. He had been urging Rylee to fund studies of basic cancer and mortality issues, complication rates, and whether silicone could cause immune diseases. But he doubted that would ever happen.

Four months later, the doctor quit. Before he left, Swanson mentioned him about implants. Dillon couldn't say for sure if he posed a risk, he told Swanson; the research wasn't complete. But he surmised that some women probably couldn't tolerate silicone—and there was no screen to identify them.

"Good luck," Dillon said. "Dow Corning is going to need a man like you." Swanson supposed it was a compliment. But he wondered just what he could do.

DOW CORNING WAS AWASH IN LEGAL PARANOIA, a small wonder. Since 1963, when it introduced breast implants, there had been mounting complaints that the devices

ruptured far more frequently than expected, that even intact implants leaked silicone, and that silicone caused myriad illnesses. In 1984, Dow Corning had lost its first major implant lawsuit; the jury, persuaded that the company had concealed problems, had found it guilty of fraud.

In 1989, after someone leaked an internal study showing "an increased incidence of fibrosarcomas at the implant site," Washington-based Public Citizen's Health Research Group had sued the Food & Drug Administration to release the results of all safety studies on silicone gel that Dow Corning had given it. In response, shortly before Dillon sent his memo, a U.S. district court judge had ordered the FDA to release the results of two decades' worth of company studies. Moreover, the judge had chastised Dow Corning for invoking secrecy orders it had won in earlier court battles to prevent him from hearing expert testimony on the studies.

The press had begun reporting that silicone leaking from implants might cause auto-immune-system diseases such as lupus and rheumatoid arthritis. And Congress was about to hold hearings on implant safety.

OVER THE COURSE OF HIS DOW CORNING CAREER, John Swanson had become, in a sense, the conscience of the corporation.

A lean, fair man who looks as though he were made to sit behind a desk in a prudent Brooks Brothers suit, Swanson joined the company in 1966, at 30, as advertising supervisor and soon became manager of industrial marketing. His break came when a speech he wrote impressed William C. Goggin, then chairman and CEO. Goggin began to have Swanson write his speeches and to seek Swanson's advice on issues such as launching a campaign to end the confusion between Dow Corning and its parents, Dow Chemical and Corning.

After Goggin retired in 1975, his successor, Jack S. Ludington, also came to rely on Swanson. Dow Corning was now deriving 45% of its nearly \$300 million in revenues overseas, and one issue that concerned Ludington was whether the company adhered to the same values in far-flung outposts as in Midland.

Public confidence in U.S. corporations had been hurt by revelations of companies bribing foreign officials and making illegal political contributions. Dow Corning hadn't been in-



volved, but it had a growing business in developing countries where kickbacks and bribes were common. In 1976, Ludington asked Swanson and three other managers to form a Business Conduct Committee to draft guidelines for ethical conduct, develop a process for monitoring business practices, and recommend ways to correct questionable activities.

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Few would consider corporate ethics riveting, and in 1976, Swanson was not among them. He considered himself more pragmatic than idealistic. He had never embraced religion. But he prided himself on his integrity, a value he felt he shared with his father, a conservative Republican who owned a grocery store in Minneapolis.

As Swanson began traveling to discuss ethics with often skeptical colleagues, he became intrigued by his task. Could a corporation reconcile the conflict between the quest for profit and socially responsible behavior? His assignment became a challenge: How do you convert ethics from simple pieties to part of the ethos of a global organization?

Swanson led the development of a code of ethics entitled *A Matter of Integrity*. The code detailed the responsibilities of the corporation and its employees and outlined proper relations with customers and suppliers. In bold type, the introduction asserted: "We will act with the idea that everything we do will eventually see the light of day."

But what distinguished the ethics program was its active and visible Business Conduct Committee, of which Swanson was the sole permanent member. The committee, staffed by top executives in rotating assignments, conducted face-to-face meetings with executives around the world that explored such sensitive topics as pricing and kickbacks. The sessions helped make ethics central to Dow Corning's culture.

What Swanson had seen as an assignment to dish out management's flavor-of-the-month became a long-term commitment. He now viewed the program as noble and informed, and with Ludington's support, he emerged as its leading proponent.

In 1984, researchers from Harvard business school undertook what became a series of laudatory studies of the program, and Swanson became a nationally recognized expert on business ethics. "John Swanson was much more genuine than most corporate ethics officers," says Laura Nash of Boston University's Institute for the Study of Economic Culture. "John had a comprehensive view that this was about a way of thinking." By 1990, Swanson, now senior consultant for communications and business conduct, was devoting nearly half his time to ethics—updating the code, making presentations to employees, and organizing and writing conduct reviews. All along, he strove to build a moral consensus that could guide employees to do the right thing.



JOHN AND COLLEEN MET IN MID-1973, THREE years after the end of his first marriage. Colleen, 34, feisty and vivacious, was also divorced and, like John, she had two children. Within four months, the couple wed.

At about the same time, a Dow Corning chemist, Silas Braley, moved into John's department. For years, Braley had helped doctors develop medical applications for silicone. Now, he was to tour the country, armed with a case full of tificial joints, ears, chins, and breast implants, promoting the use of silicone body parts. Swanson had known Dow Corning made breast implants, but working with Braley made him more aware of this small, curious part of the business.

A month or so after the Swansons married, they accompanied Braley and his wife to Detroit, where Braley was to do a radio show. During the drive, there was plenty of conversation about breast implants. Colleen asked many questions. For every one, she says, Braley had a reassuring answer. He told Colleen that if she wanted implants, he could arrange for a surgeon who was among the best at the procedure to do the operation. Subsequently, she read a Dow Corning brochure that reassured women, among other things, that implants could be expected to "last for a natural lifetime."

Says Colleen: "I had been advised by the one person who represented the best state-of-the-art knowledge of medical uses of silicone in the world. He knew the most competent plastic surgeons for this procedure in the U.S. Dow Corning had originated the silicone implants and was a highly reputable organization.... [Braley] on Si's reputation and Dow Corning's, I felt very confident that the silicone implants were safe."

So, in March, 1974, the Swansons packed Colleen's Chevrolet Impala convertible and headed for Florida. In the trunk were suitcases full of summer clothes for John, Colleen, and her two kids. Another suitcase held a box containing a pair of vacuum-sealed, sterile silicone breast implants. They were to be given to Dr. James L. Baker Jr., the surgeon chosen by Braley, to replace the ones he would stitch into Colleen. The family would go to Disney World. Along the way, Colleen would visit

Dr. Baker, who had agreed to operate for \$100 if the Swansons brought the replacement implants. Most surgeons were charging between \$1,000 and \$3,000.

The day before the surgery, the Swansons visited Dr. Baker. He took Colleen's medical history, outlined the procedure, and examined her breasts for tumors or cysts. She then signed a form confirming she had been informed of potential difficulties. The operation had been done for several years, it said, but "the end results are not and cannot be determined for a number of years to come." It also said that in a small percentage of cases, implants might not be tolerated and would have to be removed. But Baker assured her of the operation's high success rate, Colleen says, and she experienced no doubts. Colleen had surgery the next morning. Four days later, she had a final checkup. "Patient has beautiful results," Baker noted. The family headed home.

The Swansons were still newlyweds and very much in love. Many nights, they shared candlelit dinners by the fireplace. Each weekend, they'd drive to a new Michigan location where Swanson would golf with colleagues while Colleen and the other wives shopped, until they all met in evening for dinner.

Then, soon after her surgery, Colleen began suffering from dreadful migraines. A brain scan revealed no cause, and

would vanish for days, but it returned. Her doctor began giving painkillers, and an oxygen tank was placed by her bed. Her anxiety would cause her to hyperventilate.

Beginning two years later, she was beset by one ailment after another. She developed lower back pain where she had to quit her job as a dental assistant. Then came numbness in her arms and hands. Medically, rashes would render her skin as red and shiny as a severe burn. She also developed adhesive capsulitis, which caused pain and stiffness in her left shoulder.

Colleen consulted numerous specialists and underwent countless treatments, but no one could explain what was wrong. And still her ailments multiplied. She became so fatigued she could go to bed right after dinner. Then, her breasts became rock hard, and she felt a constant burning in her chest. In time, pain began to sear through her left arm and down into her ring and index fingers. Then it enveloped her hips and neck. At one point, her weight, which had been 105 pounds, fell to 89. The once healthy and attractive woman John married seemed to be dying.



## THE CONFRONTATION

*If the implants really were the cause of her problems, John thought, Dow Corning could not have known.*

*He was skeptical that silicone—which he was always told was biologically inert—had hurt her. And if she was right, he told her, “our lives will be turned upside down.”*

*“That may be,” she countered, “but I can tell you right now they’re coming out. All I care about is living.”*

*John and Colleen stayed up nearly all night, discussing what they should do. How would they find a doctor they could trust?*

MORNING IN LATE 1990—15 years into her ordeal—Colleen got a call from her daughter, now living in California. “Mom,” she said, “I think I know what’s going on with you. I just saw this man on television out here. She has all of your symptoms, and she has Dow Corning implants.” Listen—Colleen felt a great weight lift. At last, she had an explanation for her suffering.

After a long day of meetings and memos, John came home to Colleen accuse his company of selling an unsafe product that caused her illnesses. The accusation felt like a punch to the gut.

If implants really did cause such problems, he thought, the company could not have known. For that matter, he was skeptical that silicone—which he was always told was biologically inert—had hurt her. If she was right, he told her, “our lives will be turned upside down.”

“That may be,” she countered, “but I can tell you right now they’re coming out. All I care about is living.”

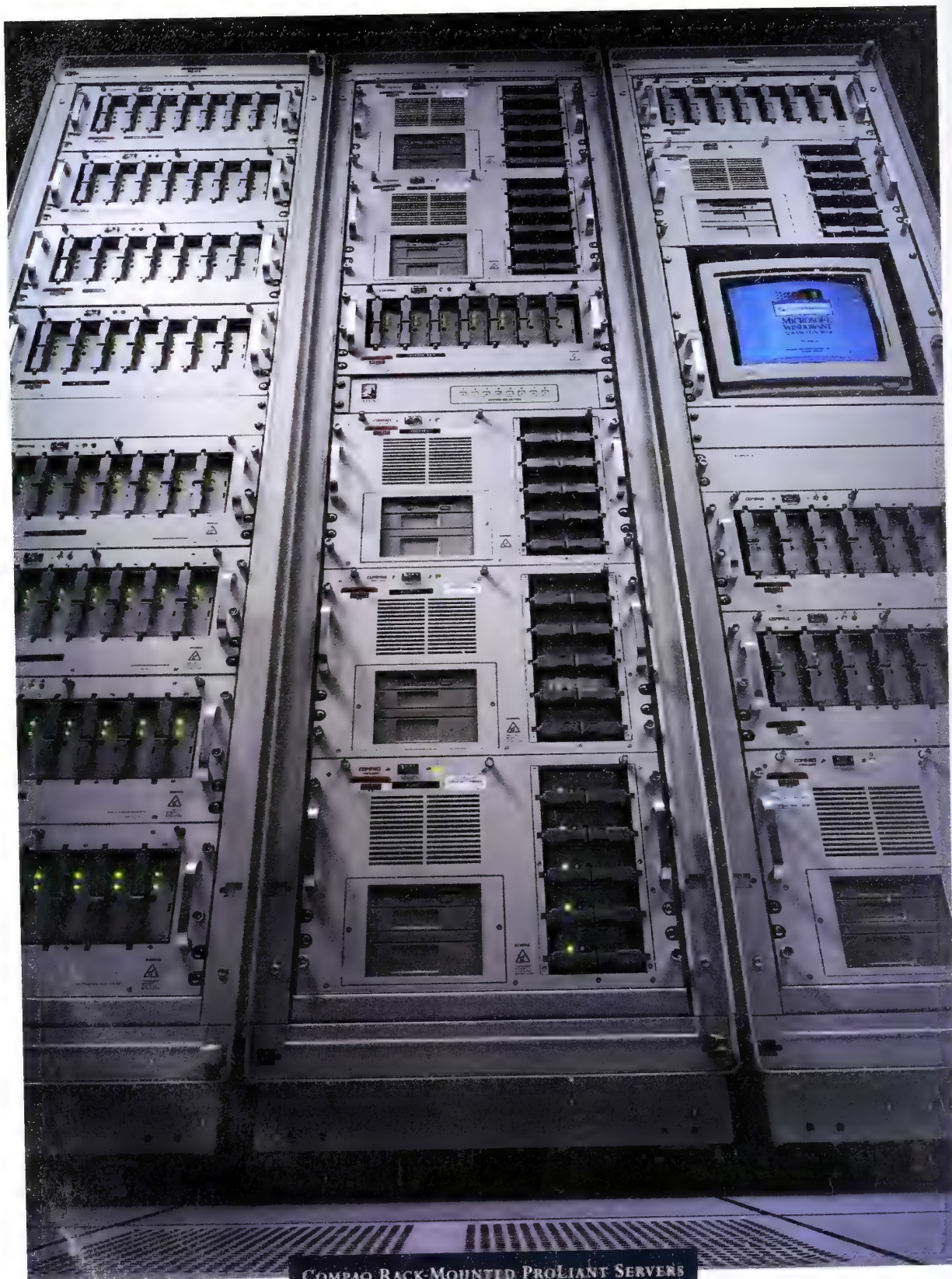
The two stayed up nearly all night, discussing what they should do. How would they find a doctor they could trust? Midland was a gossip town. Even a cursory discussion of problems with implants might get back to his colleagues. Besides, John still doubted the company was selling a harmful product. “There was no rational or documentable reason to believe it,” he says. “Intellectually, I knew where she was coming from: The pains were real—not in her head! But there were all the other, nonemotional factors that played in

it, too. We had built a good life in Midland and now suddenly all of it—friends, career—was at stake.”

That night, Colleen wasn’t all that concerned about John’s career, or their friends, or their life in the close-knit community that sometimes felt like a subdivision of Dow Corning. She knew John felt torn between loyalty to her and loyalty to the company. “Plus, he’s the one who took me to get it done.... That night was terrible. It was as if our life changed overnight. But I knew one thing for sure: I just wanted them out and I wanted to get well.”

In the weeks ahead, John felt engulfed. At work, he would listen as people around him decried the FDA’s idiotic bureaucrats and the media’s sensationalists and dismissed, often cruelly, the complaints of women with implants. At home, he would listen to Colleen, who now believed that Dow Corning had denied her the right of informed consent by hiding the risks of having implants. Back at work the next day, he’d hear the other side—that the company was the vic-





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tim of overzealous regulators and consumer advocates.

On June 28, 1991, Colleen underwent the operation to remove her implants. Afterward, her surgeon told her that her left implant had been ruptured for some time and the other was leaking silicone.



THE SAME MONTH, SWANSON READ A STORY IN BUSINESS WEEK that pushed him over the edge. Correspondent Tim Smart cited evidence that the industry had known for at least a decade of animal studies linking implants to cancer and other illnesses. He wrote that implant makers, "especially Dow Corning," were

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meeting safety questions and lawsuits "with a full-court press to keep their internal memos and studies from reaching the public." Swanson found this public questioning of the company's ethics devastating.

He immediately drafted an E-mail note to the executive then chairing the Business Conduct Committee, urging that Dow Corning reexamine its stance. "Some 20 years ago," he wrote, "Dow Chemical's intransigence about napalm gave that company a public image that took hundreds of millions of dollars and a total change in attitude to reverse. It's a lesson worth studying."

Then he began approaching colleagues to argue for suspending the production and sale of implants until the company could answer all charges. No one agreed. To others, this was about business, not ethics. Since virtually everyone in the company thought silicone was safe, it didn't make economic sense to withdraw the product. But Swanson thought the company's position was misguided even in terms of business strategy. Its strident, defensive attitude was putting its image at risk.

He went to J. Kermit Campbell, a group vice-president whom CEO Lawrence Reed had designated to manage the crisis, and recommended that a statement be prepared for consideration at an upcoming board meeting. He then wrote a news release announcing that Dow Corning would stop producing implants. Campbell took the release to the meeting but didn't fight for it, sources say. The directors were swayed by arguments that suspending operations might hurt the company in court. Besides, Dow Corning was about to deliver tens of thousands of pages of studies and other data re-

quested by the FDA to prove that implants were safe.

In July, 1991, Dow Corning shipped several cardboard boxes stuffed with documents to the agency. Little more than a month later, an FDA official denounced the clinical studies as weak that they cannot provide a reasonable assurance of safety and effectiveness of these devices."



ON SEPT. 18, 1991, SWANSON INFORMED CAMPBELL that he wanted to recuse himself from any work connected with implants. For months, he had brooded about this decision. Would he lose his job? Become a pariah? But he could no longer live with the secret that his wife was suffering from a silicone-related disease. And he could no longer accept the decision to keep selling implants.

Of course, he could have quit in protest or gone public. But he had none of the memos or safety tests that had hurt the company in court—and then been hidden by court seals. He had no scientific evidence that silicone was unsafe. For Colleen's doctors, who had treated hundreds of women

with implants, lacking proof. There were no long-term epidemiological studies. What more, Colleen's medical bills were averaging \$50,000 or more a year. John was a two years from retirement—and he loved Dow Corning. Colleen said she'd support whatever decision was made. "I didn't think he should quit," she says, "because I would prove not guilty and neither John nor I had done anything wrong."

Swanson described to Campbell Colleen's long decline and how they believed in the cause. He was asked to be recused and Campbell agreed. Swanson felt that the burden had been lifted.



### THE CEO'S RAGE

*"Look," McKennon demanded, "what does Colleen want out of this? Does she want a zillion dollars? This could be messy. Can't we just talk this out and see if we can get it resolved?" But the more the men talked, the clearer it became that they were resolving nothing.*



LESS THAN THREE months later, a California woman won a \$7.3 million judgment against Dow Corning that would be used

on appeal. Soon after, internal documents that had surfaced in the trial were leaked to FDA Commissioner David Kessler. The papers raised significant doubts about the safety of silicone implants.

On Jan. 6, 1992, Kessler called for a 45-day moratorium on sales of the implants. Soon after, Dow Corning's board began seeking successors to Ludington and Reed, neither of whom seemed capable of leading the company through the crisis. They chose Keith R. McKennon, a Dow Chemical executive vice-president who had earned the sobriquet "the fire-

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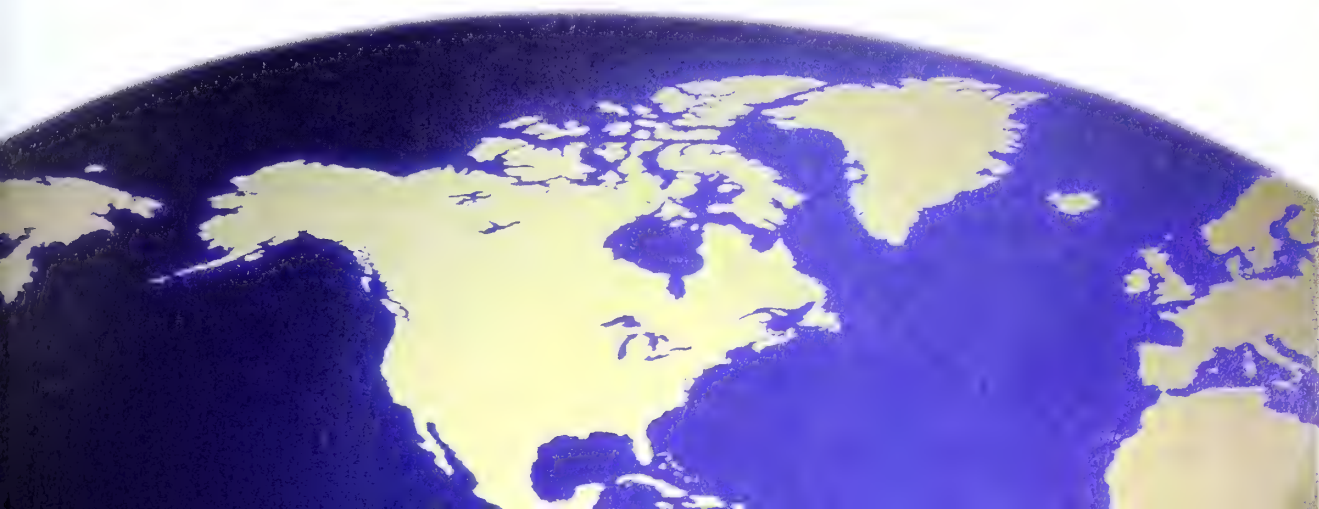
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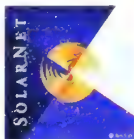
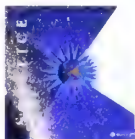
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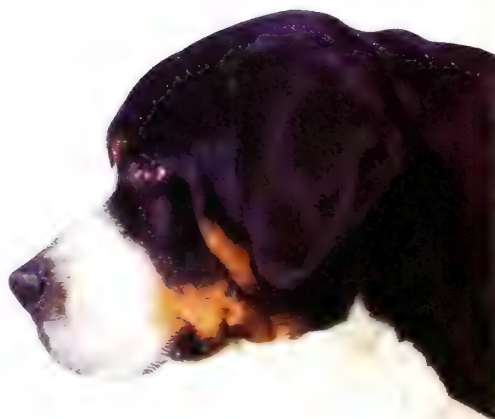
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On Feb. 10, McKennon became chairman and CEO. In March, he took Dow Corning out of the implant business. On Apr. 16, Kessler banned silicone breast implants for most women because manufacturers had not proven the devices were safe and effective.



SIX MONTHS BEFORE HER IMPLANTS WERE REMOVED, Colleen had decided to sue Dow Corning. John would not be a party to the suit nor even speak with her attorney. In January, 1991, her lawyer approached the legal department about a settlement but was rebuffed. Colleen finally sued in August, 1992, a year after her surgery. Even then, she dreaded seeing a headline about her suit, so she insisted it be filed late on a Friday.

Three months later, McKennon summoned Swanson to his office. Seeming tense and ill at ease, he told Swanson he had recently learned of Colleen's lawsuit and wished he had known about it earlier. There had been no need for a suit, he said. The company could have handled it another way.

Swanson told McKennon how the legal department had turned away Colleen's attorney. McKennon, who declined to be interviewed, clearly knew he faced a public-relations disaster if word got out. "I had never seen him this angry," says Swanson. "He was mad, first at me, and then, I suppose, at the legal department."

"Look," McKennon demanded, "what does Colleen want out of this? Does she want a zillion dollars? This could be messy. Can't we just talk this out and see if we can get it resolved?" But the more the men talked, the clearer it became that they were resolving nothing.



THOUGH HE HAD NO MORE TO DO WITH IMPLANTS at work, Swanson was consumed with them at home. He devoured any information he could find, searching for help for Colleen—and explanations for his company's behavior. He had already announced he would retire as soon as he was eligible—in August of 1993. "It was hard to put on a good face to go to work, and yet I had to do this," he says. "I did not want to appear negative or arrogant or belligerent or adversarial."

Soon after her surgery, Colleen had begun to feel better, but her fatigue, migraines, and joint pain persisted—in her doctors' view, because explantation cannot always rid the system of silicone. In May, 1993, she settled her lawsuit for an undisclosed sum.

Three months later, Swanson left Dow Corning for the last time, exiting through an underground tunnel into the summer sun. At 7 the next morning, a moving truck pulled into the Swansons' driveway. The couple was headed to Bloomington, Ind., where he hoped to establish himself as an ethics consultant. The Swansons left early the next day—skipping breakfast rather than delaying their departure. "It was a pretty day," re-

calls Colleen. "The sun was shining. I was a little numb because I was still quite ill. But I can't say I felt sad."



ON MAY 15, 1995, AFTER A U.S. DISTRICT COURT judge declared that a \$4.23 billion global settlement between implant makers and women seeking damages was inadequately funded, Dow Corning sought federal bankruptcy protection. The parent companies then wrote off their combined \$739.5 million investment in the company. Dow Corning now battling even its own insurers, who have charged the company with fraud and negligence.

Yet momentum is swinging the company's way. Recent studies from Harvard Medical School and the Mayo Clinic, among others, have cast doubt on the link between implants and disease. Critics have attacked these studies on numerous grounds—among them, that they look only for recognizable diseases, such as lupus, rather than the complex of ailments many recipients complain of. The Mayo Clinic researchers themselves cautioned that "our results... cannot be considered proof of the absence of an association between breast implants and connective-tissue disease." Ethically, in Swanson's view, the new findings are beside the point. The real issue is the company's failure to acknowledge and promptly investigate signs of trouble.

The ethical dimensions of the crisis, and Swanson's role in it, are already fodder for MBA classes in business ethics. Kenneth Goodpaster, who teaches such a course at the University of St. Thomas in Minneapolis, knows the story well.

It was he who interviewed Swanson for Harvard's flattering studies of the company's ethics program.

His students discuss the program's failure to bring problems with implants to light. They debate the merits of a legal system that lets vital information be kept from the public by a corporate seal. And they talk about John Swanson. Many question his staying at the company until he could retire.

"They see him making the right decision to leave," says Goodpaster, "but they think it took him a long time to do it. You might say that it takes some of the heroism out of it, but it also puts some of the humanity into it.... Dow Corning was John Swanson's whole life in a lot of ways. Some people could read this case and say, 'Hey, wake up, guy!' But John never claimed to be a hero. It's a story about a real human being who made an excruciatingly difficult decision. It's a personal tragedy for him and others, and it's a corporate tragedy, too."

EDITOR'S NOTE: *Informed Consent* is based on an exhaustive review of court records and documents filed with government agencies and more than 100 interviews, some with former Dow Corning Co. employees. Throughout John Byrne's search, the company repeatedly declined to let its executives be interviewed. It alleges that John Swanson once sought payment not to write a book—a charge Swanson vehemently denies. The company also asserts that John Swanson's involvement in Byrne's book "precludes the possibility of a fair, accurate, and objective evaluation of the controversy." John Swanson will receive half of any royalties. He exercised no editorial control.

## Cover Story

COMMENTARY

By Stan Crock

# WHY THE GOP HAS STAR WARS IN ITS EYES—AGAIN

The Evil Empire is dead. Washington is tightening its belt. And an Oklahoma City-style bombing is more of a threat today than incoming ballistic missiles.

Yet Star Wars—Ronald Reagan's grand vision of a high-tech shield against Soviet nukes—is back and thriving in the post-cold-war era. House-Senate budget conferees are poised to pump nearly \$1 billion next year into a national missile-defense system, \$500 million more than President Clinton wants. The money, to fund new ground-based weapons, satellite sensors dubbed "brilliant eyes," and possibly space lasers, is a down-

payment on a program that could cost an additional \$7 billion to complete by 2016, the Congressional Budget Office says.

The saga of Star Wars' resurrection shows the resilience of high-concept ideas in Washington—no matter how often they're ridiculed. And the criticisms of Star Wars are endless: It won't work. It's pork. It will undermine arms-control efforts to deal with the most serious threat—Russia's thousands of warheads. And the country can ill afford it.

But philosophy, politics, and profits have dovetailed to propel the project forward. With a stream of disturbing reports as their ammo, Reaganites and conservative think tanks have publicized the threat from such rogue states as North Korea and

Iraq. Republicans, relying on polls and focus groups, think voters will go ballistic if Democrats block efforts to provide a defense blanket. Meanwhile, arms makers such as TRW Inc. and Lockheed Martin Corp. could reap a bonanza from one of the Pentagon's few growth areas.

**"WACKOS."** That's quite a turnabout for Star Wars, which dropped off the radar screen when the GOP left the White House. From a peak of \$1.9 billion in 1992, funding plummeted to about \$400 million after President Clinton took office. The Clintonites emphasized guarding against short-range missiles, such as Scuds used in

the Persian Gulf War. "A Star Wars missile defense is not a priority in an austere budget environment," declares one top Administration official.

The campaign to revive Star Wars began in 1994, when stalwarts concluded the White House was doing little about the proliferation of biological, chemical, and nuclear weapons by emerging states. "Wackos are getting these dangerous weapons and the means to deliver them," says Frank J. Gaffney Jr., a Pentagon official during the Reagan Administration. In 1994, Gaffney helped assemble more than 80 conservative Star Wars supporters who issued a broadside warning of the new dangers.

At the same time, the GOP decided Star Wars was an irresistible political issue, and they included support for such a system in the Contract With America. "Defense and foreign policy were seen as areas of particular vulnerability for the Clinton Administration," says GOP pollster J. Steven Wagner.

Pork politics was also a key factor. At a House hearing in January, Representative Jane Harman (D-Calif.) expressed what was on the minds of many lawmakers who represented struggling defense contractors. A national missile-defense system "is critical to the industrial base of my district," she said.

Still, there were rifts between the think-tankers and the pols. The Star Warriors' game plan would pave the way

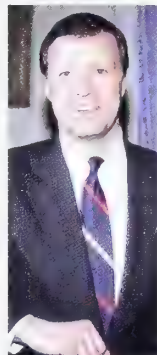
## AN IRON TRIANGLE HAS REVIVED STAR WARS...



### REAGANITE HARD-LINERS

Now ensconced in Washington think tanks, ex-Reagan Administration officials such as former Strategic Defense Initiative Chief Henry Cooper have issued a stream of

reports and studies detailing new ballistic-missile threats to the U.S. and justifying a missile-defense system.



### REPUBLICAN CONGRESSMEN

A national missile-defense system was part of the House GOP's Contract With America. And Republicans in both chambers, such as Christopher Cox of California, are

pushing for more funding and deployment of a scaled-back Star Wars program—risking veto by President Clinton.



### DEFENSE CONTRACTORS

With the Pentagon's budget under tight constraints, missile defense is one of the few growth areas. Weapons makers such as CEO Joseph T. Gorman of TRW, along with Boeing, Lockheed Martin, and others, could reap a windfall from contracts for the system, which could cost \$48 billion by 2016.

## ...AND DEFIED THE BUDGET LAW OF GRAVITY



DATA: BUSINESS WEEK, CONGRESSIONAL BUDGET OFFICE



to restore Reagan's original vision: repudiate the 1972 Antiballistic Missile (ABM) Treaty, which limits strategic defenses; build satellite sensors and ground- and space-based interceptors; and deploy them quickly. Because the Administration is focusing on defense against short-range rockets rather than faster long-range weapons, if North Korea launches a missile, "a captain on a cruiser can defend Tokyo, but not Seattle," gripes Henry F. Cooper, a former Pentagon official. "That's stupid."

The pols had a different concern: They couldn't line up enough votes for a comprehensive Star Wars scheme. So Republicans proposed something far more modest, aimed at defense against a limited attack from, say, Libya. Initially, the components would be just ground-based weapons and space sensors. Space-based weapons might be added later.

**DEPLOYMENT NOW?** The thorniest issue was the ABM Treaty. Arms-control supporters argue that more funding for Star Wars would provoke a nationalistic Russia to reject sharp reductions in nuclear weapons under the proposed START II Treaty. They also contend that smuggled bombs are more of a worry than missiles. "Ryder trucks are a much better way of getting your point across," says arms-control expert Jack Mendelsohn.

Such arguments carried weight with Democrats in the Senate, which increased funding for Star Wars—but for development, not deployment. Now, the GOP has two choices: With a compromise bill such as the Senate's, they can pass legislation the President will sign. Or they could opt simply to embarrass the Democrats by adopting the tough House version, which would prompt a filibuster or Clinton veto. "There is virtue in making sure we all understand who wants to defend America and who doesn't," says one GOP aide.

Either way, Star Wars advocates and their supporters on Capitol Hill believe they're in control. The GOP is counting on a more solidly Republican Congress—and possibly a Republican White House—in 1996 to finish the job. If they're right, the question isn't whether Star Wars will be built, but how fast.

*Crock covers national security from Washington.*

## People

### DEALMAKERS

# TEAM DISNEY'S UNKNOWN STARS

It's Bollenbach and Litvack who'll make the ABC deal go



**ODD COUPLE?** Bollenbach (left) is a risk-taker, while Litvack is more cautious

**B**y now, the tale is familiar. Walt Disney Chairman Michael D. Eisner, on a stroll in Sun Valley, Idaho, chances upon Thomas S. Murphy, his counterpart at Capital Cities/ABC Inc. After a few pleasantries, Eisner suggests a merger, and when Cap Cities investor Warren E. Buffett gives his blessing, a \$19 billion deal is on its way.

A nice story. Too bad it's a bit of a fairy tale. In fact, for months before the second-largest merger ever was announced, Eisner huddled with key executives to put the gears in motion. With him in Idaho were two team members, Sanford M. Litvack and Stephen F. Bollenbach, perhaps Hollywood's most powerful unknown executives. "The two Michaels are getting all the attention right now," says a Walt Disney Co. veteran, referring to Eisner and new President Michael Ovitz, "but Eisner is counting on

these other two to make the place go."

Eisner has acknowledged as much establishing that Litvack, chief of corporate operations, and Bollenbach, chief financial officer, will report to him, not Ovitz. How that will work is not clear, but chances are that as Eisner and Ovitz tend to the creative aspects of forging a \$22 billion media colossus, Litvack and Bollenbach will take on the responsibility to make the parts work in sync. "We envision this as a team operation," says Litvack. "In some companies, they have an office of the president very similar to this."

Bollenbach, who joined Disney in April, is a onetime surfer who grew up in Southern California, worked a summer at Disneyland, and drives a \$113,000 Ferrari Testarossa. Litvack, a "walk-on" football player at the University of Iowa who transferred to the University

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Connecticut after a knee injury, grew up in Brooklyn, is a grandfather of five, and strives for anonymity. He was thrust into his current role by the 1994 death of President Frank G. Wells, who had hired him three years earlier as general counsel, and by the departure last spring of studio boss Jeffrey Katzenberg.

Today, Litvack and Bollenbach occupy adjacent offices, galvanized as a team by the ABC deal. When Bollenbach came aboard, the merger idea was already under intense scrutiny, he says. He attended four meetings on it, including one just days before Eisner flew to Idaho. At that meeting, when Eisner asked who would help run the combined company, Litvack jotted Ovitz' name on a napkin and slipped it to the CEO.

After the Idaho meeting, Bollenbach and Litvack led the team that put the deal together. Bollenbach, who had prodded the debt-averse Eisner to take on new debt to do the merger, pressed Eisner to seek an all-cash deal, but Murphy initially held out for all stock, Bollenbach recalls. "Our stock has great currency," he says, "and I think the Cap Cities folks knew that as well." By phone three days after their first encounter, Eisner and Murphy split the difference: Disney will pay half stock, half cash.

**RAISED EYEBROWS.** The final agreement took shape during a weekend of late-night negotiations with ABC executives. The Disney team successfully pressed two key issues: a \$400 million payment to Disney if another bid were accepted and a separate agreement for Disney to supply ABC with programming. Sources say Litvack also urged a quick resolution to the \$10 billion libel case Philip Morris Cos. had brought against ABC. That may explain the speed with which ABC agreed to a settlement.

Litvack is no stranger to big-league transactions for Disney. As general counsel, he and then-CFO Richard C. Nanula last year handled the often prickly negotiations with representatives of Saudi Prince Alwaleed bin Talal bin Abdulaziz Alsaad, who invested

## STEPHEN F. BOLLENBACH



**TITLE** Senior executive vice-president, chief financial officer

**AGE** 53

**JOINED DISNEY** Apr. 4, 1995

**PREVIOUS JOBS** President and CEO, Host Marriott, 1993-95

CFO, Trump Organization 1990-92

CFO, Holiday Corp. (now Promus)

VP, finance, Ludwig Group

Chairman and CEO, Southwest Savings & Loan

**EDUCATION** BS, UCLA; MS, Management, University of California at Northridge

Ludwig and Donald Trump. His career has been marked by risk-taking. In 1986, as CFO of Holiday Corp., he fought off a Trump takeover with a \$1.6 billion special dividend to shareholders, then piled on debt to make the company a major hotel developer. Four years later, he helped Trump avert bankruptcy by refinancing his huge debt load. Bollenbach, Trump says now, is "not afraid of debt, and so far, at least, he's shown he knows how to keep out of its way, too."

Litvack and Bollenbach first met earlier this year at a game of Disney's Anaheim Mighty Ducks hockey team. Bollenbach was still chief executive of Host Marriott Corp., a 100-hotel unit that he helped create in 1993 when Marriott Corp. split into two companies. Bollenbach subsequently moved to Disney at the urging of board member and former CFO Gary Wilson, who had worked with him at Marriott. Soon afterward, he and Litvack were added to the Disney board.

Because Disney's theme parks generate

\$350 million in ailing Euro Disney. Litvack first represented Disney during his mid-'80s tenure at the New York law firm Donovan, Leisure, Newton & Irvine. Before that, he was the Carter Administration's assistant attorney general in charge of the Antitrust Div. Then, ironically, he signed consent decrees prohibiting ABC and CBS from merging with Hollywood studios. "Different times, different policies," he shrugs now.

If Litvack is the cautious lawyer, Bollenbach is more a buccaneer of the balance sheet, who has worked for such high-profile financiers as the late shipbuilder Daniel K.

so much cash, Bollenbach soon began preaching the wisdom of borrowing and he quickly won a convert. "I know all the arguments about debt and tax advantages," says Eisner, "so I spent a couple of weeks learning about debt and then go out and spend \$1 billion with it to buy a company." Bollenbach, working with a bank consortium led by Citibank, put together the \$10 billion line of credit that will be presented to Disney's board Sept. 1. He and Litvack have been shuttling between New York to meet with Cap Cities and start the transition. So far, they say, they have focused on merging administrative functions. But in time, company sources say, they'll look at cutting costs by merging TV production and foreign operations.

**CROWDED HOUSE.** Disney's behind-the-scenes strategists are likely to become even less visible once Ovitz comes aboard Oct. 1 and after Cap Cities finally joins the family. While Litvack has been negotiating with Katzenberg, who threatened to sue for money he says Disney owes him, that task will pass to Ovitz, say insiders. Ovitz will also be charged with finding programming for the Disney-led consortium of telephone companies eager to send entertainment down their wires.

Meanwhile, the merger is expected to close in 1996. Shaping the new company will probably fall squarely on Eisner for now. "No matter how you look at these two guys, any company still has to be a reflection of its chairman," observes

## SANFORD M. LITVACK



**TITLE** Senior executive vice-president, chief of corporate operations

**AGE** 58

**JOINED DISNEY** April, 1991, as general counsel

**PREVIOUS JOBS** Member of Executive Committee, Dewey Ballantine 1986-91

Chairman, Executive Committee, Donovan, Leisure, Newton & Irvine 1983-86

Assistant U.S. Attorney General, antitrust division, 1979-81

**EDUCATION** BA, University of Connecticut; LLB, Georgetown Law Center

former general counsel Joe Shapiro, Litvack's longtime partner, who introduced him to Eisner and Wells. Another former Disney executive says Ovitz and Litvack will split Wells's role, with Litvack acting as COO and Ovitz handling high-profile deals and working with creative talent. Bollenbach will focus on financing. Does it sound as if it's getting a little crowded in Disney's executive suite? Could be. But that's a big improvement over a company that, just months ago, was ridiculed for having management depth.

By Ronald Groves in Burbank, Calif.

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## MEDICARE

# HOW TO HEAL MEDICARE

Surgery is scheduled. Recovery depends on shrewd reforms

**D**r. James A. Block's forehead creases with worry as he contemplates the future. His 1,702-bed Johns Hopkins Hospital is one of the top research and teaching centers in the country. And so far, Hopkins has managed to avoid the layoffs bedeviling so many other teaching centers. What's worrying the hospital's president and CEO is "this enormous experiment, this great risk we're about to undertake."

A new heart transplant technique? No. The hand-wringing is over the Medicare reforms that congressional Republicans want to enact. "I just wish Newt would call me and say, 'Actually, I'm not going to gut your education and research programs or cut off your most vulnerable patients.'"

Like thousands of other health professionals around the country, Block is watching the Washington policy debate with emotions that run from hope to horror. Fully half of Hopkins' revenues come from Washington and subsidize education and research. Even the smallest program changes would ripple throughout the entire health-care industry.

Welcome or not, change is on the way. Medicare, the \$178 billion federal program serving 37 million elderly and disabled, is going under Congress' knife in the next few weeks. Cuts in Medicare spending are the key to GOP plans to balance the budget and provide \$245 billion in tax breaks over seven years. To pay for this, Medicare would be cut by \$270 billion, or 14%, over seven

years. House Speaker Newt Gingrich (R-Ga.), the man in Dr. Block's nightmares, insists that cutting the program can be accomplished in the name of reform.

While the GOP hasn't yet settled on a plan, many health professionals agree the system needs an overhaul. "If we don't make the changes now, it will be late in the 21st century," says Dr. Dallas Henley, president-elect of the American Academy of Family Physicians. "Medicare has not been evolving in the market."

**RUSHING CHANGE.** But any reform worthy of the name will have to be carefully crafted and fully discussed. A clumsy revamping could easily jeopardize cancer research and postpone cures for sickle-cell anemia, and a hundred other maladies. The GOP leadership would like to rush their changes into law this year after a brief debate. But that's unlikely since lobbyists, Democrats, and moderate Republicans have yet to wince in on Gingrich's proposed changes. The battle is more likely to mirror the

**SMALL COMFORT**  
Despite Medicare's runaway costs, "the benefits package still says a former Reagan official



ted fight health-care in 1994. Republicans choose an route: a big Medicare cuts to doc- d hospitals t raising pocket

## REHAB TIME

Most doctors don't want cuts just to balance the budget but say Medicare must be brought up to date

for the vocal elderly. The political battle rages, BUSINESS WEEK culled some of the best prems for fixing Medicare from doc-administrators, managed-care nations, economists, and other ex- (table). Most don't want to see re cut merely to balance the bud- t nearly all want to see the 30- program brought up to date. The us: The most sensible solutions n market incentives to lower the medical care through competition insurers and providers.

**HY SENIORS.** The experts also hat government can't stand back the private sector run the show. Regulators will have to step in to that cost-cutting doesn't mean will be treated like second-class s. The elderly will also have to be d about the intricacies of picking a bewildering array of managed- ans, such as health maintenance ations and preferred provider or- ions. Further, government needs urage the tiny nursing home in- industry. Whether

to buy such insur- s often a senior's import decision. gton must also ne teaching hospi- modernize their specialists to keep n the nation's rapid to managed care. family physicians, in- s, and generalists e needed as the call ch specialists as esiology fades.

Medicare's expen- wing out of control, ncial underpinnings ve to be addressed. e healthier seniors ing longer, the age edicare eligibility to be raised to at 7 to keep pace with dual increase in So- ecurity retirement nd a consumption ould be substituted e highly regressive tax that hits young s the hardest but



doesn't touch even the wealthiest of seniors. Wealthier seniors—those with incomes over \$45,000—should pay more for their coverage. And ultimately, the nation will have to engage in frank debate about the rationing of health care—limiting the use of advanced surgical techniques, life-sustaining machinery, and elective surgery for those unable to benefit substantially.

There is little disagreement on how American health care got to this point. Since Medicare and Medicaid were enacted in 1965, the industry has seen a tremendous boom in size, technology, and cost. The elderly benefited most. A

flowering of technology helped push life expectancy from 70 to 76. The over-65 population rose from 9% of the total in 1965 to 12% today. Half as many Americans now die from heart attacks, a third as many from strokes. "We went through three decades of phenomenal growth, but we weren't paying attention to affordability and accessibility," admits Dr. John D. Stobo, vice-dean of Johns Hopkins' school of medicine.

Indeed, the advances came with a terrific price tag. Half of all health inflation over the past 20 years is due to technology improvements, says Congress' Office of Technology Assessment.

Even the simplest devices got gold-plated. "Everything now is disposable, and all the instruments have digital readouts," complains Dr. Jeffrey P. Koplan, president of the Prudential Center for Health Care Research in Atlanta. "What was wrong with the old mercury thermometers?"

Congress added to the inflation by expanding Medicare benefits and keeping premiums and deductibles low. Kidney dialysis, for example, was added to the benefit mix along with care for the disabled. Naturally, Medicare's costs exploded. To keep pace, Congress repeatedly boosted Medicare's payroll tax (charts). Still, costs outstripped income. The Medicare trust fund that pays for hospitalizations is headed for bankruptcy in 2002.

Aside from Medicare's runaway cost and the

## No Single Cure for Medicare

As Congress wrangles over ways to overhaul the massive health-care program for the elderly, Business Week picks a handful of prescriptions that, taken together, add up to effective reform:

**VOUCHERS AND MEDICAL SAVINGS ACCOUNTS** Encourage competition among health providers and insurers by giving seniors the money to pay for their chosen plans.

**QUALITY CONTROL** Educate consumers about trade-offs between quality and cost control. Set standards for managed-care providers.

**MEANS TESTING** Charge affluent seniors higher premiums, co-payments, and deductibles for Medicare.

**DOCTOR GLUT** Cut federal subsidies for foreign medical students and for medical schools that generate too many specialists in fields where they're already in oversupply.

**NURSING HOMES** Standardize current thicket of private insurance for long-term care, which Medicare doesn't cover but which the elderly desperately need.

**CONSUMPTION TAX** Ease Medicare's payroll-tax burden on young workers by substituting a sales tax.

**RAISE ELIGIBILITY AGE** Match Medicare to rising life-expectancy rates. Otherwise, financial problems will multiply and the burden on workers will grow.

DATA BUSINESS WEEK



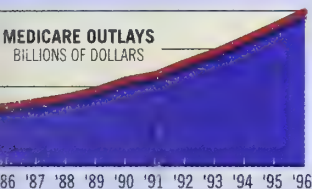


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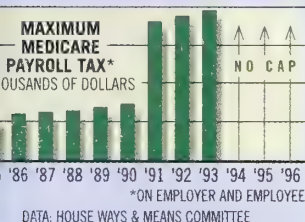
## ocial Issues

all tax's drag on the economy, is another problem: "The benefit package stinks," says Deborah L. Steel, a former Reagan Administration official and now an expert on entitlements. Medicare doesn't pay for the first day of hospitalization or the copay, doesn't cover eyeglasses, dentures, hearing aids, or prescription drugs. Worse, it doesn't cover most long-term home care, a growing burden on the elderly and their children.

### AS MEDICARE COSTS EXPLODE...



### ...THE TAX BURDEN GROWS



Republicans hope they have an answer to Medicare's skimpy benefits. The plan aims to expand coverage by allowing providers and insurance companies to compete for the elderly's business. The elderly would shop among a variety of new forms of insurance companies, alliances of doctors, HMOs, and managed-care providers.

**EMPLOYEE POWER.** Here's how one such plan using government vouchers, might work. Seniors would be given a voucher to shop among private insurance plans and providers. Adding in a little of their own money, retirees could buy basic insurance. Or they might choose to go to a company that offers higher levels of coverage for a higher premium—say, an HMO that offers some prescription coverage and vision care. The senior gets a choice of plans, the government puts a cap on its per capita spending, and market forces are brought to bear on runaway costs.

The voucher could be turned into a savings account and deposited in a tax-free Medicare Savings Account similar to an Individual Retirement Account. Suppose, for example, the value of the Medicare premium was for \$4,800, the current av-

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off we will all be," says Dr. Da-  
. Sundwall, president of the  
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## cial Issues

beneficiaries happy by expanding and to keep Medicare solvent automatically raising taxes. But critics status quo say the tax remedy is wise nor fair. That's because the ization portion of Medicare is by a payroll tax. That puts the burden on young workers benefit of the retired elderly, incomes are generally higher but ect to the tax.

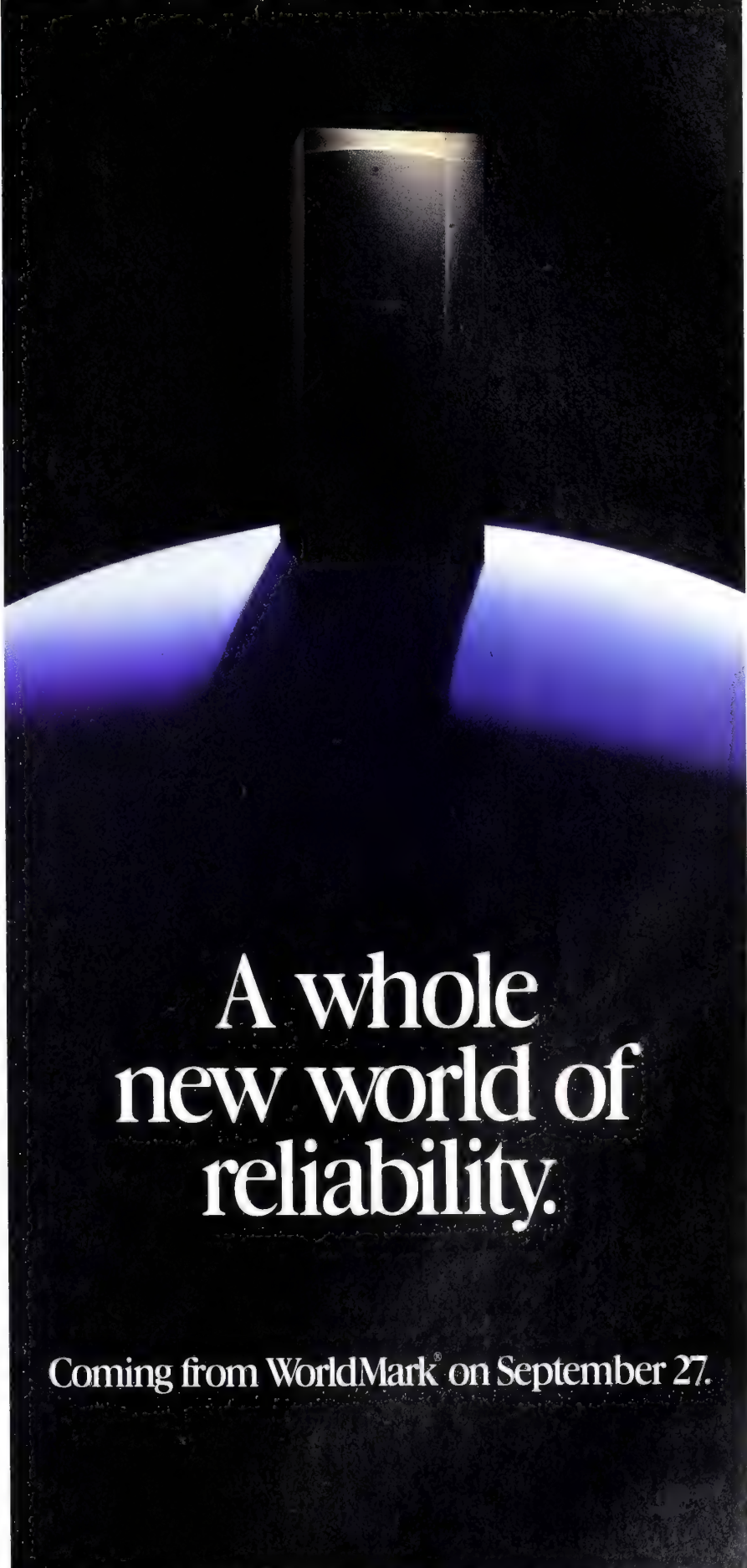
The hardest issue is rationing: Limiting medicine to seniors could truly benefit

higher premiums, co-payments, deductibles for the top-earning 10% ors. A consumption tax could shift some of the burden onto wealthy-ees. "The fact is, Medicare is the government's most popular program, but the financing has got to change," says Robert D. Reischauer, director of the Congressional Budget Office.

**W**ING UP. The hardest issue is one that the health industry likes to avoid: rationing, or what professionals sometimes refer to as "utilization management." In plain English: limiting care to those seniors who could truly benefit. Hence, no hip-replacement surgery for the 90-year-old nursing-home resident who doesn't walk anywhere. "An efficient health-care system must employ wholesale rationing," says Princeton University health economist Uwe E. Reinhardt. "It is time for America to grow up and understand what will happen" as we turn much of the Medicare system over to the private sector.

Options such as these—the most difficult kinds of choices for government and for families—will eventually have to be faced as technology continues to advance and push costs higher. In the meantime, most experts believe that health care inflation can be kept to a fairly manageable level. But just as Dr. Fuchs and his researchers have helped make health care the best in the world, they have also made it the most expensive. It may now be time for Dr. Fuchs and his researchers to find ways to keep Americans healthy and not break the bank.

by Paul Magnusson in Baltimore



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NETWORKING

# 3COM IS SHOWING A LOT OF HUSTLE

It's the fastest-growing player in networking hardware

**E**ric A. Benhamou, chief executive of 3Com Corp., says he knew all along there would be a backlash from sports fans when he agreed to a deal with the city of San Francisco to change the name of Candlestick Park to 3Com Park on Sept. 8. He's getting more than he bargained for: from ill will in the Bay Area to nationally syndicated cartoons that deride the obscure company's rush for the spotlight. "We're trying to bring the networking industry out of its shadow, and I knew we would have to break a few eggs in the process," says the soft-spoken CEO, happily noting the 40 mentions of 3Com on NBC's nationally televised 49ers game on Sept. 10.

Sports fans are just finding out what Wall Street and the folks in Silicon Valley already know: 3Com is one of the fastest-growing players in the red-hot market for networking hardware. From simple circuit cards to exotic switches, 3Com makes the gear that corporations rely on to move data between PCs, larger computer systems, and other devices such as printers. After a three-year buying binge—including the July 27 deal to pay \$775 million for rival Chipcom Corp.—3Com has quadrupled in size.

Sales for the year ended May 31 reached \$1.3 billion (not including Chipcom's \$267 million in revenue), putting it right behind Silicon Valley rival Cisco Systems Inc., the leader in the \$15 billion network equipment industry.

3Com already sells the widest range of products. It dominates the market for the interface cards that attach PCs to networks and for certain types of "hubs" used to connect networks in smaller businesses and remote offices. After spending \$1 billion on 10 acquisitions, Benhamou says he is putting together the pieces that will make 3Com a one-stop global networking supermarket. "This is incredibly complicated stuff, and customers want to buy everything from one company," says Noel P. Lind-

**3Com's consumer push includes cards that let home PCs use ultrafast data services**

**PUSHY?** Sports fans are indignant over the renaming of Candlestick

sey, a Hambrecht & Quist Inc. arb. In the latest quarter, ended Aug. 1, revenues rose 64% to \$430 million; earnings doubled, to \$59 million. In fiscal 1996, analysts expect a 26% increase in per-share earnings.

Benhamou sees an even wider market for 3Com. He wants to spawn new markets serving small businesses and consumers. By 2000, he says, his initiatives could bring in 60% of revenue. That's a bold goal, given that folks building public networks—and cable companies—have yet to figure out how and when they'll bring high-speed connections to consumers. Benhamou's strategy is to be ready for what they build so he can sell what's needed to replace today's modems and give consumers data at speeds rivaling the corporate networks. Given the Internet craze, says Benhamou, "I can't see this won't happen."

**SHOPPING LIST.** So far, the plan has raved on Wall Street. Revenues more than tripled since 1992, even before the Chipcom acquisition. Despite annual price drops of 10% on network cards, 3Com's gross margins have actually risen from 40% in mid-1993 to around 55% in the quarter ended Sept. 19. Adjusted for split, stock price has streaked from \$28 in September, 1992, to around 43 now.

What sets 3Com apart in the re consolidating networking market is its unmatched ability to make acquisitions work. The credit goes to Benhamou, a man who "knows how to buy companies," says Thomas J. Pincince, a senior analyst with Forrester Research in Cambridge, Mass. "It's almost

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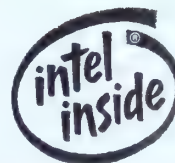
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he's got a checklist he goes down."

In fact, 3Com has a database of 140 possible acquisition candidates and tracks everything that happens in those companies, down to personnel changes. The secret to takeover success, says Benhamou, is to offer a corporate vision that's at least as compelling as the founders' original dream—either in price, work environment, or societal impact. As a result, "If we know about a deal and make a similar bid as others, we'll win the bid every time," he gloats.

Benhamou learned about takeovers

Sephardic Temple in Silicon Valley.

The technical knowhow has paid off. Take network cards, once regarded as a dead-end business. Benhamou invested heavily in custom chips that add features, improve reliability, and lower costs. He also added seven \$10 million production lines that can beat Asian job-shops on cost. 3Com's share of the network card market has doubled to 40%-plus and analysts figure its gross margins on the cards exceeds 40%. Another plus: its manufacturing prowess has helped the company jump quickly into new markets, such as stackable hubs used to con-

ber, it plans a pilot program for small networks to very small business CompUSA stores. These setups will be company with a few PCs share a printer and pass around E-mail just like the corporate crowd.

It will be up against Cisco's CiscoPro line, slated for introduction Sept. 27. The line will include packages for hooking telecommuters to the corporate network or speeding up Internet access. "We'll take a leadership position very quickly," vows Cisco CEO John Chambers. He figures small-business consumer sales could reach \$300 million

## 3Com's Buying Binge

*After three years of acquisitions, it now tops a billion dollars in sales*

**1987** Buys Bridge Communications to get into the market for bridges and routers used to connect corporate LANs.

**1992** With British-based BICC Group PLC, gains a customer base in Europe.

**1993** Buys Star-Tek Inc. for \$43 million and gains

its IBM-standard network products. Pacific Monolithics brings wireless technology.

**1994** A busy year. Centrum Communications, a \$36 million deal, brings in products for remote access to corporate networks. For \$59

million, 3Com buys Israel-based NiceCom Ltd., maker of speedy asynchronous transfer mode (ATM) switches. Synernetics Inc., acquired for \$104 million, gets 3Com into LAN switches.

**1995** Another binge: Access Works Com-

munications, acquired for \$240 million, makes ISDN equipment for PCs. Sonnet Communications acquires Primary Access Corp. bought for \$174 million and \$70 million respectively, let 3Com sell ISDN gear for phone companies. The capper: the \$75 million bid to acquire Chipcom.

the hard way when he was called on to fix the fractious merger with Bridge Communications that brought him to 3Com in 1987. A co-founder of Bridge, Benhamou watched as 3Com moved away from its core PC add-in card business to develop network server computers to run software being jointly developed by IBM and Microsoft Corp. When the alliance blew up in 1989, 3Com was left in a bind.

After the board nudged out co-founder and President L. William Krause, Benhamou launched a turnaround plan that involved rebuilding the circuit-card business and using 3Com's still healthy balance sheet for acquisitions to add new technology and expand distribution. He laid off 12% of the company and scotched the computer-making effort in early 1991.

Benhamou is well-suited to the re-engineering task. Krause says he brought Benhamou on board in part because of his calm and even style. "To pull a company through a transition, that's what you need." His technical background didn't hurt either. An Algerian raised in France, Benhamou helped install the first Internet site at Stanford, where he received a master's in electrical engineering. He's not all techno-geek, though. Benhamou is an avid guitarist and helped found the only



**CEO BENHAMOU:** He "knows how to buy companies"

net branch offices to corporate nets.

The next phase may prove a bit more difficult, especially since 3Com keeps bumping into Cisco. The market leader has mainly focused on corporate sales, while 3Com has used dealers to reach a variety of customers. Now, Cisco plans to attack the low end of the market. It forged a deal with Compaq Computer Corp. to resell its IOS network-management software on Compaq's server PCs, and has plans to sell network interface cards as well.

Now the two are locking horns in the consumer market. In early September, 3Com brought out \$495 circuit cards, sold at California's Fry's Electronics stores, that let home PCs use high-speed ISDN data services. In Octo-

ber, it plans a pilot program for small networks to very small business CompUSA stores. These setups will be company with a few PCs share a printer and pass around E-mail just like the corporate crowd.

It will be up against Cisco's CiscoPro line, slated for introduction Sept. 27. The line will include packages for hooking telecommuters to the corporate network or speeding up Internet access. "We'll take a leadership position very quickly," vows Cisco CEO John Chambers. He figures small-business consumer sales could reach \$300 million

in a year. He readily acknowledges that 3Com can leverage its PC expertise to grab 10-20% of the new markets, but insists Cisco can lock up as much as 40% because of its in corporate network.

**NET BREAKS.** Benhamou is taking his message directly to the people. Today's PC users are begging to be connected, he says. In addition

exhibits at 3Com Park (eight Internet kiosks for mid-inning cyber-surfing) 3Com is undertaking high-profile community projects, including wiring public schools in San Jose, Calif., England, Ireland. Marketing Vice-President M. Roberts is planning the company's first TV ads.

That's only part of the plan. Benhamou has filled his board with executives who can help guide the expansion beyond business networks, including James Barksdale, CEO of high-flying browser developer Netscape Communications, and Pacific Telesis President David W. Dorman. With a vast consumer market as the prize, it's a new ball game for 3Com.

*By Peter Burrows in San Francisco*



BY NEIL GROSS

## FOOTPRINTS' FOOD MONITORING

THOUSANDS OF PEOPLE FALL sick each year from salmonella and other bacterial pests. In 1993, a major outbreak in the mid-Atlantic region of Mexico killed 47 Californians. To detect the bugs early, they're time-consuming and often inexact.

DuPont Co. is developing technologies that could help the company's Ribonox, which went on sale in 1993, processing companies this year for \$10, scans a coliform bacteria taken from a food sample, isolates a DNA "fingerprint" through a technique called electrophoresis, and compares it in a database with hundreds of similar bacterial patterns. The process of identifying a bacterium involved culturing, growing them in petri dishes, and studying their growth—a routine that took five days. The Ribonox can do it in as little as four hours and also helps tell bugs snuck in through food materials or spread in contaminated processing equipment, says DuPont scientist Scott L. Rakestraw.

DuPont's gene sleuths will take a step further. They have begun to commercialize use of polymerase chain reaction (PCR)—made famous by the O.J. Simpson trial—can quickly multiply small quantities of suspect DNA fragments on samples. For just \$10 a test, the technology, DuPont licensed from Amn-LaRoche Inc. and Elmer Corp., can positively identify traces of salmonella in one day. Similar to troubling types of bacteria and listeria are under development.

## BIG BARBIE IS WATCHING YOU

NASA'S DREAM OF CHEAP, BATTERY-POWERED CAMERAS ON chips that can beam pictures back from space may first be realized in a more earthbound setting: children's toys. Los Angeles designer Curtis M. Brubaker wants to put one-chip video cameras in dolls, remote-controlled cars, and robots. These would send signals back to a receiver that plugs into the TV set or VCR so kids can monitor or record what their toy tanks, trucks, and robots "see" as they explore the living room or terrorize the cat. Brubaker has won two key patents on a real-time video transmission scheme and on the use of wireless video in toys.

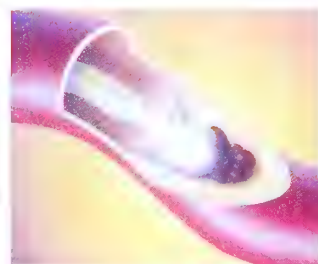
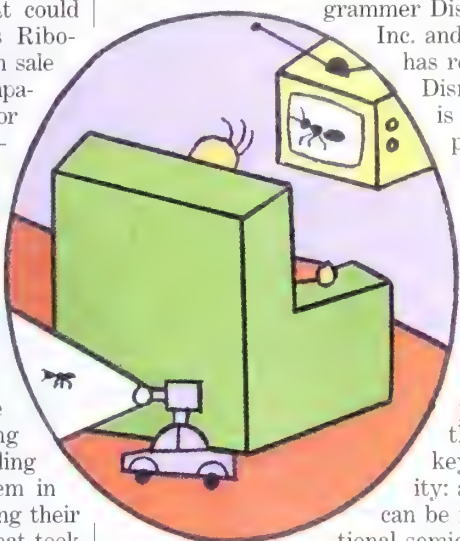
Development so far has been funded by cable-TV programmer Discovery Communications

Inc. and Walt Disney Co., which has registered the trademark DisneyVision. Now, Brubaker

is looking for a technology partner to underwrite the design of the communications chip. The first product would be a starter kit that includes a receiver and a cigar-size camera and communications module—all for just \$99. Licensed toy-makers can then create products that incorporate the plug-in camera. The

key to low cost and portability: a new sensor chip that can be manufactured in conventional semiconductor facilities. Brubaker has also shown a color version for theme parks

and institutions, including a remote-controlled toy submarine camera that captures close-ups of marine life in aquariums.



## INNOVATIONS

■ Scientists at Los Alamos National Laboratory are helping doctors at St. Vincent Hospital & Medical Center in Portland, Ore., save lives with their military laser expertise. They're beaming light through catheters to zap blood clots in arteries (illustration). Hemoglobin in the clots absorbs the light and dissolves, thanks to a photochemical process that doesn't damage surrounding tissue.

■ Teams of genetic engineers are racing to clone spider silk, one of the strongest and most elastic materials. Until recently, attempts had produced only fragmentary molecules. But scientists at Lebensmittel Consulting of Fostoria, Ohio, and Plant Cell Technologies of Chatham, Mass., claim to have cloned complete proteins. Their work, which is backed by the U.S. Army, could yield a new generation of lightweight body armor.

## TRAPPING THE TOMATO MOTH—WITH SEX

BRAZIL HARVESTS ABOUT 2.2 million tons of tomatoes a year and exports them around the world. Unfortunately, it must spray about 70% of the crop with chemical pesticides to hold larvae of the voracious South American tomato moth at bay. Even then, bugs sheltered in leaves can survive the dousing and destroy the crop.

Cornell University scientists believe they can eliminate the need for 90% of that spraying. They've identified

and synthesized a pheromone—a natural sex attractant—secreted by the female moth. Placing it in traps in recent tests in Brazil, they succeeded in capturing thousands of male moths in a single night. "Normally, we would be happy if we trapped a few hundred," says Cornell chemistry professor Jerrold Meinwald, who heads an international team of researchers.

The first hurdle was obtaining the natural phero-

mone from female moths, which release it for only 30 minutes during the day. Traditional gas chromatography and mass spectroscopy provided the first glimpse of the molecule's unusual structure. Scientists fine-tuned their understanding through a new technique that involves putting the molecule through chemical transformations. The team then synthesized the pheromone and applied for a patent. Meinwald says the new mode of chemical analysis could help researchers to characterize pheromones from other pests.



## SEMICONDUCTORS

# THE GREAT SILICON RUSH OF '95

Billion-dollar chip factories are sprouting all over

Calling it a spending binge hardly suffices. Try orgy. The semiconductor industry is throwing money at new, big-ticket chipmaking plants at record rates. In September alone, Fujitsu, Hitachi, Motorola, SGS-Thomson Microelectronics, and a partnership of Toshiba and IBM announced plans to build five chip plants at a cost of \$6 billion. And Samsung Group will join the billion-buck crowd any day now.

All told, 90 new wafer-fabrication factories, or "fabs," will come on stream this year and next. These 90 plants will have cost more than \$75 billion to build. That's more than the industry invested during all of the 1980s.

Chipmakers are following a prudent guideline: Those who plow the most into new production facilities win. That's how the Japanese edged out the U.S. in the 1980s—and how the U.S. came back in the 1990s. And it's how other chip suppliers in Asia, especially South Koreans, hope to grab market share. They're now outspending everyone else (chart).

**MEMORY HOGS.** The coming tide of new capacity may be one reason why investors are skittish about high tech. But the gurus don't see overcapacity problems for several more years. Daniel L. Klesken, a veteran chip-industry analyst at Robertson, Stephens & Co., has hiked his long-range forecast four times over the past 12 months. He now pegs chip sales in 2000 at \$350 billion, up 175% from his prediction of a year ago.

One reason: Intel Corp.'s latest micro-

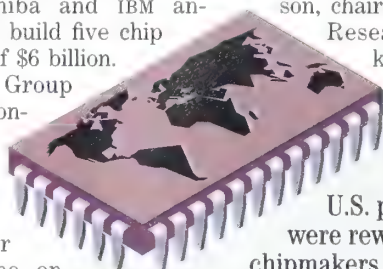
processors and Microsoft Corp.'s new Windows 95 operating system are memory hogs. New PCs need two to four times as much dynamic random-access memory (DRAM) as older PCs. "We didn't think Win95 would have much effect on DRAM demand," admits Jerry D. Hutcheson, chairman of market-watcher VLSI Research Inc. in San Jose. He knows better now.

No matter where you

can produce rapid market-share gains. Now, Korean electronics giants, such as Samsung Semiconductors Inc., are following suit, says George Burns, president of Strategic Marketing Associates in San Diego, Calif. Once Samsung decides to take the lead in DRAMs, he says, "it's a pretty straightforward proposition to figure out how much they had to spend to get there."

**NEW CONFEDERACY.** The companies increased their capital budget steadily in the last 10 years, and in 1994 climbed to the No. 1 spot, eclipsing such heavyweights as NEC Corp. and Toshiba Corp. Dataquest Inc. figures that Samsung is investing nearly \$2 billion in new capacity this year. Only three makers are spending more: Intel Corp. at \$3.5 billion; Motorola Inc., at \$2.3 billion; and Korea's LG Group (formerly LG star), which is making its own bid for a bigger slice of the action, with an investment of \$2.1 billion.

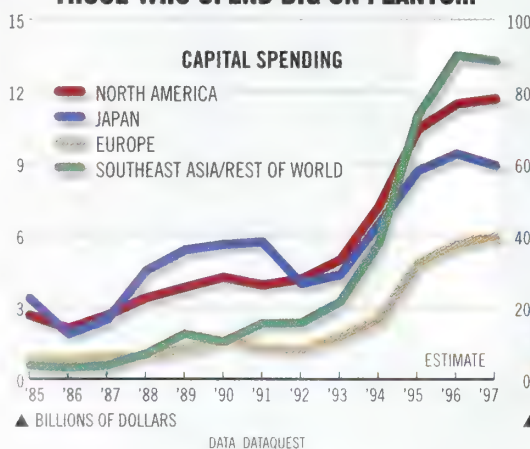
But Samsung seems ready to



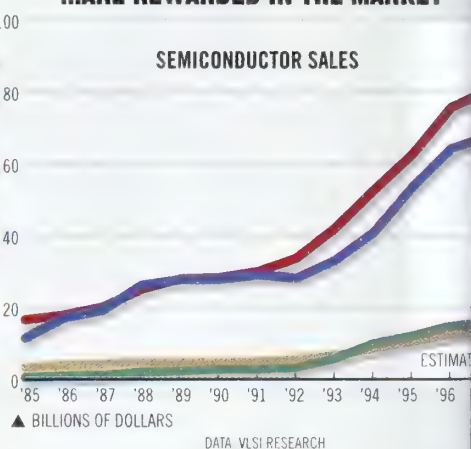
## Chipmaking's High Stakes

U.S. producers anted up billions more than Japanese rivals, and were rewarded over time with bigger market share. Southeast Asian chipmakers now spend even more and will grow the fastest.

### THOSE WHO SPEND BIG ON PLANTS...



### ...ARE REWARDED IN THE MARKET



turn, the story is the same: "We don't see any abatement in this insatiable appetite at least through 1997," says John Luke, president of TSMC USA Inc., the U.S. arm of Taiwan Semiconductor Manufacturing Co. TSMC broke ground last April for a \$1 billion fab in Taiwan and already plans another, its fifth, because demand exceeds supply by at least 20%. Concedes Kevin J. McGarity, senior vice-president and head of worldwide marketing at Texas Instruments Inc.: "We are basically out of capacity."

U.S. chipmakers showed early this decade that investments in new capacity

its bet again. Instead of breakeven ground for one new wafer fab each year, says Mark Ellsberry, marketing president for Samsung Semiconductor in San Jose, the company is "highly likely" to start a new chip factory every 18 months. The next one will be a \$1 billion fab in the U.S.

The U.S. is clearly the hottest ground for gigabuck chip plants. While a few behemoths are under construction in Asia and Europe, at least a dozen are in the works in the U.S., including three by Intel and two by Motorola, not counting the Austin fab



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that Motorola just opened. One of these new plants is destined for an unusual chipmaking location: Virginia. It will crank out PowerPC microprocessors in Richmond, just down the road from the \$1.2 billion plant that IBM and Toshiba will build in Manassas.

All the spending by U.S. chip producers is helping the American companies that supply the exotic equipment

## "We are basically out of capacity," reports Texas Instruments. So are other chipmakers

used to make chips. VLSI Research figures U.S. suppliers have 51% of that \$24 billion market, vs. 42% for Japanese rivals. By 2000, when the equipment business could top \$45 billion, VLSI predicts U.S. suppliers will have 55%. The chip-equipment industry is also on a spending spree—developing the next generation of chip systems while cranking out all the equipment needed by the new wafer fabs. Japan's Nikon Corp. is expanding its chip-equipment business by \$3 billion, and Applied Materials Inc. in Santa Clara, Calif., says it will pump as much as \$500 million into new technology by 1999.

**CAPITAL CRUNCH?** Around that time, some chipmakers may find themselves running into a capital crunch. The projected cost of a chip plant at the start of the new century is \$3 billion—and still climbing. "There is concern about the increasing cost of wafer-fabrication plants," says Steven R. Appleton, president of Micron Technology Inc. In fact, some industry leaders—including Intel Chairman Gordon E. Moore—worry that the ante required in the next decade could soar beyond the reach of all but a handful of companies.

For now, chipmakers are basking in the longest boom in the industry's history. The chip business used to gyrate every few years, with prices sometimes plummeting 50% in six months. The consensus is that those roller-coaster days are gone forever, thanks in part to close working relationships between chipmakers and their customers. Furthermore, when the current PC boom in the U.S. and Europe slows down, there's a whole world of developing nations that will need PCs, cellular telephones, and all sorts of electronics hardware. Which means that money invested now won't go to waste.

By Otis Port in New York and Michael J. Parks in Seattle

## Marketing



### LUXURY CARS

# ACURA: STUCK BETWEEN GEARS?

It's banking on a "prestige" pitch to rescue lagging sales

**A**cura came roaring into the U.S. luxury market in 1986, and things haven't been the same since. It was an audacious experiment by Japan's Honda Motor Co. to see if Americans would pay a then-unheard-of \$20,000 for a Japanese car. Its pitch? A premium car at a bargain price compared with European luxury imports. The first TV ads from Acura talked of "precision-crafted automobiles" and pictured shocked German executives reading the news in their papers. For four years in a row, Acura topped the prestigious J.D. Power & Associates Inc. customer-satisfaction awards, and it quickly became the best-selling premium import brand.

But the road has become a lot rockier since then for Acura, which accounts for 15% of Honda's North American unit sales. With results off 25% in the first eight months of 1995 and headed for their worst full-year showing ever, Acura is desperately trying to retool its image. New advertising stresses luxury and prestige instead of engineering and performance as a way to justify prices that are no longer markedly below the competition. But the first ads infuriated dealers, who demanded and got a share

of the regional ad budget. And Acura is still searching for a way to get de-pinned by falling sales, to spruce up their 10-year-old showrooms. Meanwhile, the line's well-established brand names Legend and Integra, will soon be replaced by models identified by letter and-number combinations in order to shift the brand focus to Acura.

**HEAVY TRAFFIC.** As long as it underprice competitors in the luxury market, Acura's sales hummed. But in 1992, European luxury brands such as Mercedes, BMW, and Audi started raising their inflated prices. That, along with the rising yen, wiped out some of Acura's advantage. Archrivals Toyota Motor Corp. and Nissan Motor Corp. had launched their even-more-upscale brands—Lexus and Infiniti—in 1989 with full-size sedans starting at \$20,000 and dealers famous for coding buyers.

The combination slammed the brakes on Acura sales, which peaked in 1991. "Acura led the Japanese charge into the premium luxury segment," says John G. Jacobs, president of market researcher Jacobs & Associates Inc. in Rutherford, N.J. "But they've been outmaneuvered by Lexus and Infiniti, and



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## Marketing

didn't anticipate the resurgence of the European luxury brands." Adds Thomas G. Elliott, executive vice-president at American Honda Motor Co.: "We came to find out that, in the luxury-car market, performance isn't enough. The buyers want status, prestige, comfort, and luxury."

So far, though, Acura has had a hard time convincing buyers that they'll get enough of those attributes to justify prices that can top \$40,000 on the Legend. Acura dropped the old "precision-crafted performance" ads with the 1994 models in favor of a campaign that featured mansions with cobblestone driveways and a towel-draped woman getting a massage in a gazebo. The new tag line: "Some things are worth the price." Dealers dubbed them the "Channel" ads. Nissan rushed out a parody

plus Lexus and Infiniti models, the TL with a smaller engine the RL will sell for \$10,000 less. Acura introduced its TL series this summer, including the \$28,000 2.5TL and the \$33,000 3.0TL. The idea is that Legend buyers will be shocked over prices that start at \$34,000 and can trade down to the TL series without leaving the Acura brand. Acura will introduce a luxury sport-utility, a redesigned Isuzu Trooper renamed the Acura SLX, for about \$30,000 in December and next spring will add the CL coupe for about \$25,000.

**CUSTOMER-HANDLING.** It will take more service as well as new luxury products to win over customers. But getting a commitment from the dealers who provide that service could be the most difficult part of Acura's transformation. Last year, it started away

from top dealers free of charge, based on customer handling scores rather than pure sales numbers. This year, it hired Sandy O'Connell, which trained Saturn and Infiniti dealers, to teach Acura dealers how to win buyers. So far, more than half of Acura's 283 dealers have gone through the unitary program. It's working: Acura has rebounded to No. 4 in the J.D. Power satisfaction rankings, where it once dominated: It outperformed Lexus, Infiniti, and even ahead of Mercedes, BMW, and Cadillac.

Now, Acura must persuade dealers to upgrade to the wood-and-marble trim of today's luxury dealerships. "If you're going to be a luxury franchise, you've got to look like a luxury franchise," says Stephen P. Cushman, president of Automotive Group, which owns dealerships in San Diego and Escondido, Calif. "We've got to deliver the message that they're projecting." That was tough when dealers' sales are at a time low and a quarter of Acura dealers are losing money. Acura hopes to help an upgrade program it can roll out in stages.

But Acura will soon have one more advantage over its Japanese competition: production in the U.S., starting with next spring's CL coupe. Against the strong yen will give Acura an edge over Infiniti and Lexus, which are both made in Japan. The new image and new image can't hurt, but in the end, it may be plain old lower prices that rev up sales at Acura.

By Larry Armstrong in Los Angeles



that claimed its \$13,000 Altima was "worth far more than the price."

Ads for 1996 models continue to hit hard on the luxury theme. "Acura gets extremely high marks for quality, dependability, and value, but it doesn't perform well in categories like luxurious, expensive-looking, and prestigious. We have to change the image," says Timothy W. Hart, executive vice-president of Ketchum Advertising in Los Angeles. New promotions, such as an 18-month tour with Cirque du Soleil, are meant to get the word out, too. But customers are likely to get a mixed message. To appease dealers, Acura is shifting one-third of its \$40 million regional ad budget to regional dealer associations, which traditionally run hard sell, rather than image, ads.

Acura is also changing and renaming its products. The Legend name will disappear next spring, to be followed in a year or two by the Integra. Acura will replace the Legend with the 3.5RL, a bigger, more luxurious car designed to compete with top-of-the-line, \$50,000-

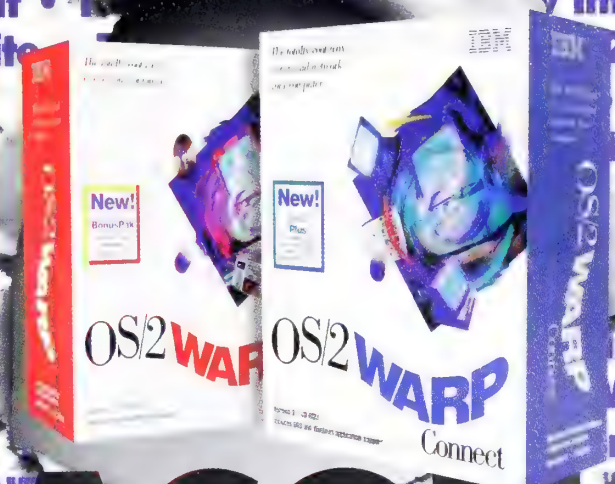
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EDITED BY AMY DUNKIN

## MEDICINE DISCOVERS A NEW ALLY: THE CLOCK

If asthma attacks are most likely to occur in the middle of the night, doesn't it stand to reason that medication administered before bedtime would be most effective? And if the risk of stroke is greatest between 6 a.m. and 10 a.m., shouldn't hypertensive individuals take blood-pressure drugs in doses that would prevent early-morning surges?

For chronobiologists, who study biological functions in relation to time, the answers to such questions have long been apparent. To them, the human body is a symphony of rhythms in which rising and falling blood pressure, heart rate, hormone levels, and temperature are part of a highly integrated and time-sensitive interplay.

Applied clinically, chronobiology uses what is known about the body's cyclical processes to recognize and treat disease. Michael Smolensky, director of Hermann Hospital's Center of Chronobiology & Chronotherapeutics in Houston, says health is a "synchrony of all the biological rhythms within the human body." Thus, any cycle—sleep/wake, menstrual, hormonal—that demonstrates rhythmic abnormalities indicates biological discord, better known as illness.

**OFFBEAT RHYTHMS.** Thanks to technology, mapping the body's rhythms and discovering any aberrant beats is easier and less expensive today. Ten years ago, the 24-hour monitoring crucial to clinical chronobiology would have meant constant surveillance and repeated pokes and prods by a team in lab coats. But



**HEALTH**



new computerized de-  
cluding wristwatch-  
sensors and pock-  
-pressure and heart  
s, make it possible to  
ine patients' cyclical  
ions without disrupt-  
r daily routines.

Chronobiology has been the  
most important factor  
growth of clinical chro-  
gy over the past  
rs," says Dr. Franz  
g, a researcher at  
iversity of Minne-  
ronobiology Labor-  
alberg coined the  
chronobiology in  
owadays, he says,  
ream doctors can  
ously track their  
s' biological activ-  
er extended peri-  
not rely on single,  
a-time measure-  
-which amounts to  
snapshots of a roll-  
er."

has implications for  
ent as well as diag-  
because, as with bio-  
rhythms, illnesses  
ndulate. Studies  
at rheumatoid ar-  
flares up at night,  
attacks typically oc-  
the morning, and  
cells vary in their  
according to sea-  
time of day. As a  
chronobiologists pay  
h attention to tim-  
therapeutic inter-

as to choice of thera-  
fore now, we've always  
ow to treat. Today, we  
so ask when to treat,"  
sky says.

**PROTECTION.** For ex-  
blood pressure natural-  
up in the early morn-  
the body readies itself  
e the day. But this in-  
the risk of heart at-  
nd stroke for people  
eart problems or high  
pressure. Thus, Dr.

Portman, a kidney  
ist and researcher at  
ermann Center, says hy-  
ive patients can often  
tter results and even  
wer doses of medica-  
they target its adminis-  
to prevent dangerous,  
g pressure surges.

Clinical trials have also  
proved that anti-inflammatory  
drugs to combat asthma and  
rheumatoid arthritis are more  
effective if given at night,  
when levels of the body's in-  
herent anti-inflammatory  
agents, such as the hormone  
cortisol, fall. Such strategic  
dosing dramatically reduces  
the likelihood of nighttime

lignant and malignant changes  
on the surface cells of the cer-  
vix occur more frequently in  
the summer months. And of  
the two most common types  
of testicular cancer, the  
growth of one peaks in De-  
cember-January, the other in  
August-September. Hrushesky  
says these rhythms suggest  
false negatives would be less

explains Smolensky. "The goal  
is to administer them during  
those windows of time when  
they will do the most harm  
to the cancer but the least  
harm to the patient." And  
with the advent of pumps  
that deliver intravenous drugs  
at preprogrammed times, he  
says, such timed treatments  
are now possible without  
hospitalization.

Chronobiology also has  
applications in the man-  
agement of sleep and  
mood disorders. "In these  
situations, bright light is  
often of great benefit,"  
says Dr. Daniel Kripke,  
professor of psychiatry at  
the University of Califor-  
nia at San Diego. He "re-  
sets body clocks" by ex-  
posing his patients to  
bright light at specified  
times during the day. Such  
light therapy seems to  
regulate the hormonal cy-  
cles that strongly affect  
sleeping and emotions.  
There is also early evi-  
dence that precisely timed  
light therapy reduces con-  
fusion in the elderly and  
regulates menstrual cycles.

While proponents claim  
chronobiology is a field  
that is limitless in its  
breadth, it also is a field  
with few players. Only a  
handful of chronobiology  
clinics are operating in the  
U.S. and Europe, and

many deal exclusively with  
sleep disorders. But more  
mainstream doctors are in-  
corporating chronobiology  
into their practices, and big  
medical centers, such as Brigh-  
am & Women's Hospital in  
Boston and the University of  
Pittsburgh School of Medi-  
cine, are using its techniques.  
The National Institutes of  
Health has funded several  
studies on the subject. Also,  
chronobiology conferences are  
drawing hundreds of health-  
care professionals rather than  
the sprinkling of erudite re-  
searchers who showed up in  
years past. "Chronobiology is  
taking off in the world of  
medicine," Smolensky says.  
Time, after all, is on its  
side.

Kate Murphy

## Tracking the Body's Cycles

|                   |                                                                                                                                                                                                 |
|-------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>1:00 A.M.</b>  | <ul style="list-style-type: none"> <li>Pregnant women are most likely to go into labor.</li> <li>Lymphocytes (white blood cells) are at their peak.</li> </ul>                                  |
| <b>2:00 A.M.</b>  | <ul style="list-style-type: none"> <li>Growth hormone levels are highest.</li> </ul>                                                                                                            |
| <b>4:00 A.M.</b>  | <ul style="list-style-type: none"> <li>Asthma attacks are most likely.</li> </ul>                                                                                                               |
| <b>6:00 A.M.</b>  | <ul style="list-style-type: none"> <li>Onset of menstruation is most likely.</li> <li>Plasma insulin is lowest.</li> <li>Blood pressure and heart rate begin to rise rapidly.</li> </ul>        |
| <b>7:00 A.M.</b>  | <ul style="list-style-type: none"> <li>Symptoms of allergic rhinitis (hay fever) are worst.</li> </ul>                                                                                          |
| <b>8:00 A.M.</b>  | <ul style="list-style-type: none"> <li>Calories are burned most readily.</li> <li>Risk for heart attack and stroke is highest.</li> <li>Symptoms for rheumatoid arthritis are worst.</li> </ul> |
| <b>10:00 A.M.</b> | <ul style="list-style-type: none"> <li>Gastrointestinal bleeding is most likely from ulcers.</li> </ul>                                                                                         |
| <b>NOON</b>       | <ul style="list-style-type: none"> <li>Level of hemoglobin in blood peaks.</li> </ul>                                                                                                           |
| <b>1:00 P.M.</b>  | <ul style="list-style-type: none"> <li>Serum cholesterol peaks.</li> </ul>                                                                                                                      |
| <b>3:00 P.M.</b>  | <ul style="list-style-type: none"> <li>Grip strength, respiratory rate, and reflex sensitivity highest; a good time for athletics.</li> </ul>                                                   |
| <b>4:00 P.M.</b>  | <ul style="list-style-type: none"> <li>Body temperature, pulse, and blood pressure peak.</li> </ul>                                                                                             |
| <b>6:00 P.M.</b>  | <ul style="list-style-type: none"> <li>Urinary flow is highest.</li> </ul>                                                                                                                      |
| <b>9:00 P.M.</b>  | <ul style="list-style-type: none"> <li>Pain threshold is lowest.</li> </ul>                                                                                                                     |
| <b>11:00 P.M.</b> | <ul style="list-style-type: none"> <li>Skin is most reactive; allergic responses more likely.</li> </ul>                                                                                        |

DATA: BUSINESS WEEK

asthma attacks and diminish-  
es the swelling of joints and  
stiffness that arthritics notice  
upon awakening.

Also asking "when to  
treat" is Dr. William Hrushesky, senior attending oncologist at the Samuel Stratton Veteran's Administration Medical Center in Albany, N.Y. Hrushesky has been caring for cancer patients chronobiologically since 1979. "The importance of timing in the screening and treatment of cancer cannot be overemphasized," he says.

Several international popu-  
lation studies indicate that  
cancer growth rates vary sea-  
sonally. Breast-cancer cells  
tend to be most active in  
spring and less in fall. Prema-

likely if cancer screenings  
were done "in-season."

Furthermore, biological  
rhythms can help determine  
when to schedule therapies  
once cancers are discovered.  
Hrushesky has published a  
study that indicates women's  
breast-cancer surgeries are far  
more likely to be curative if  
performed in the middle of  
their menstrual cycles (the  
week following ovulation). His  
ongoing investigations show  
that patients respond better  
to chemotherapy and radiation  
administered at certain times  
of the day or week. The actual  
schedule varies, depending  
on the type of cancer as well  
as the therapeutic agent.

"The toxicity of cancer  
drugs varies rhythmically,"



## COMPUTER TUTORS TO HELP YOU ACE THE SAT

I approach most journalistic tasks with enthusiasm. So why did an assignment to

evaluate software aimed at helping high school juniors and seniors prepare for the Scholastic Assessment Test make me cringe? The answer, of course, is that no matter how old you are, you never forget the pain of taking an exam that can make or break your dreams of getting into the right college.

Yet having reacquainted myself with algebra, analogies, and quantitative comparisons, I can report to parents of college-bound youths that most of the programs I explored may well ease your son's or daughter's jitters. And with the next exam (formerly called the Scholastic Aptitude Test) scheduled for Oct. 14, there may still be time to lift their scores.

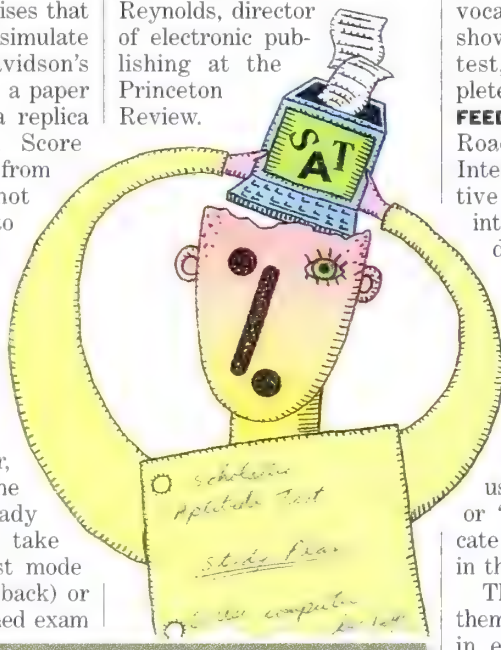
**DIAGNOSTIC TESTS.** The SAT programs for Windows and Macintosh PCs range from the no-nonsense Cliffs StudyWare for the SAT I from Cliffs Notes, to The Underground CD-ROM Handbook for the SAT, a rather annoying (to this grownup, anyway) effort from Swfte International and Workman Publishing, billed as providing "unauthorized techniques to deliver your best SAT score ever." The program features animated caricatures of four real-life Ivy League students, but I felt like I was getting tutored by Beavis and Butthead. Zelos Digital Learning's Team SAT also uses student mentors, but in video clips instead of cartoons. My favorite programs came from Davidson & Associates, Kaplan Interactive, the Learning Co., and the Princeton Review.

The great promise of multimedia software is to personalize an interactive learning experience not possible in a tutorial book. As students take diagnostic practice tests, the top programs can analyze their strengths

and weaknesses and prescribe learning exercises that best suit them. To simulate the experience, Davidson's software comes with a paper test booklet that's a replica of the real thing. Score Builder for the SAT from the Learning Co. not only asks students to answer questions but also queries them on how they arrived at their responses. Then the program maps out a study plan that emphasizes the skills they need to master, without wasting time on stuff they already know. Students can take practice tests in test mode (timed, without feedback) or tutor mode (an untimed exam

with immediate explanations.)

Any software is vastly cheaper than Kaplan's and the Princeton Review's SAT prep classes, which cost up to \$700. And students can work at their own pace and schedule, though any score hikes will be related to how much time a kid puts in. (Kaplan says three to four hours a week for six weeks is basic, though 12 weeks is better.) Still, if you can afford it, "a good review course will always be better than a good software program," says Jim Reynolds, director of electronic publishing at the Princeton Review.



The main menu on Princeton Review's fine side the SAT and PSAT pro is an animated high school corridor. (The shorter PSAT the preliminary version of SAT and qualifies student National Merit Scholarship. Students can click on a with such labels as "very math," and "tests." Be the "guidance counselor" they can compare results practice tests to the average scores needed to get into schools. The program identifies 300 commonly vocabulary words it show up repeatedly on test, such as "abhor," "plete," and "surfeit."

### FEEDBACK FEATURE.

RoadTrip 96 from Kaplan Interactive uses an intuitive dashboard as its interface menu screen.

Students can personalize their study plan based on how much time they have before the exam, after some practice exams, get excellent feedback on their testing habits. During diagnostic practice users can click on a "or "unsure" button to cate how confident they in their answers.

The Kaplan program them know how well they in each category. It track of the number of a correct answer changed to the wrong answer and an incorrect answer made right. And it tells students the five longest time took to come up with a correct answer, and five longest times on a wrong response. On pacing, Kaplan recommends students spend 60 seconds on easy questions, 45 to 75 on medium ones, 60 to 90 seconds on the test choices. With Kaplan's program comes a separate college-search software and a link to Kaplan on America Online, where students can download sample questions and a diagnostic practice test for free. let's see, if  $2X - 5 = 9$ ,  $3X + 2 = \dots$  Edward

## Grading SAT Prep Software

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**YOUR PERSONAL TRAINER  
FOR THE SAT**  
DAVIDSON, \$35

COMMENTS

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Has sense of humor that may appeal to youths. Uses video lessons and animation to make rote topics fun.

Customizes study plan based on how long student has to prepare for exam. Includes link to America Online.

Comes with paper test booklet to simulate real exam. When students are puzzled by questions, they can click on strategies button for tips.

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DATA. BUSINESS WEEK





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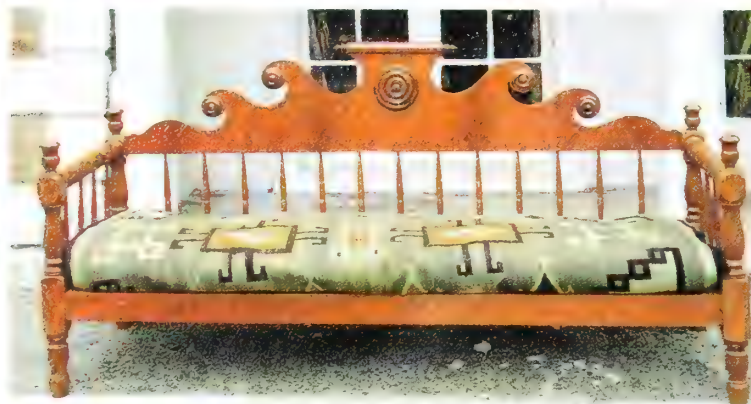
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**SETTEE:** Prices can reach \$6,000

## THE LATTER-DAY BOOM IN MORMON ANTIQUES

Members of the Church of Jesus Christ of Latter-Day Saints who trekked across the prairie to Utah in 1847 were in search of religious freedom, not a new lifestyle. So they took a chunk of Victorian life with them, reproducing even the ornate furniture they had left behind. "They were trying to create culture in a desert," says Marilyn Conover Barker, author of *The Legacy of Mormon Furniture* (\$29.95, Gibbs Smith), due out Oct. 1.

Today, that culture brings high prices. Californians discovered 19th century Mormon furniture—characterized by its exaggerated dimensions and hand-painted wood grain—a decade ago. But now it's catching on with East Coast designers and collectors of religious folk art.

Mormon furniture's appeal, says New York decorator Timothy Macdonald, is its "rustic quality and a sense of whimsy that comes through the interpretation of pioneer craftsmen." He assembled a collection for Lionel Pincus, chairman and chief executive of E. M. Warburg Pincus. Yet most collec-

tors are individuals snapping up items for a few hundred dollars each.

Salt Lake City dealer Jonathan Sweet (801 359-4852) says good Mormon pieces "should appreciate the way Shaker furniture has." Prices, increasing some 10% a year, should continue to go up. A top-grade rocker by an anon-



**OCTAGONAL DESK:** Soft woods required oversize legs

ymous craftsman that sold for \$500 five years ago now fetches \$3,500, and a museum-quality settee costs \$6,000, a fourfold increase. But you can buy a Windsor chair for as little as \$65, or a pedestal table for \$300. F. Weixler (801 534-1014) re-

stores authentic furniture and custom-builds reproductions for about 40% of the price of old pieces.

While a limited amount of furniture was made from 1847 to the turn of the century, pieces are still coming onto the market as dealers scour barns and out-

buildings. Most Mormon furniture is still sold through Utah dealers, who have a pipeline into small towns across the state. But if you know what to look for, you can find items in antique stores in adjacent states as well as California. Since the Saints are known for keeping every scrap of paper from pioneer days, pieces are often documented. "Ask for the grandma story," advises Mormon-furniture specialist John Told in Midway, Utah (801 785-5224).

Mormon furniture has nothing to do with religion, although an occasional piece uses a beehive or other church symbol as a design element. Instead, the

furniture, much of it made by English and Scandinavian converts, copied conventional styles—but with a difference. Utah had no hardwood. Carpenters made do with cottonwood and pine, woods so soft they compensated by making oversize legs to support the weight of tables and chairs. "Proportions are cartoony and fun," explains Told.

Most surfaces were painted, often with ox blood, or grained to produce the look of hardwoods, such as walnut and mahogany. Faux oak graining, used in both church woodwork and furniture, was called "Brigham oak" for church President Brigham Young, himself a carpenter and grainer. In the 1970s,

when natural woods were popular, many Mormon were stripped of their painted grain, decreasing value up to 90%. They're highly collectible, though cause of their styling.

**WIDE ROCKER.** Look for tees and daybeds that can to accommodate two or three sleepers. They are marked a country Empire style with a pediment in back. Rockers are popular, especially oversize "Brigham rockers" contrived when a furniture maker asked the Youngs to make an impractical rocker to fit the church leader's dimensions. Also popular are grained floor sugar bins.

Finely made furniture craftsmen such as

### FURNITURE

Ramsay, Dinwoodee

William Bell bring twice the price of anonymous works. Pieces stamped "Brigham Works" also bring a premium. They were made by converts working in their own shops to offset transportation costs to

Occasionally, Mormon furniture was constructed of hardwood that arrived in Utah as packing crates. Recently sold a New York collector what he calls a "mite settee." It was made from a packing case stamped "dynamite"—a word con-

say could apply to all Mormon furniture. Sandra

### WORTH NOTING

**JUNIOR INVESTORS** If your kids know what type of mutual fund to invest in a single industry or who was America's first billionaire? They find out by playing the Young Investor Game, a free interactive computer program from Liberty Financial Cos. You can request a disk, which works in DOS or Windows, by calling 800 KIDS. (The answer to the question is the investor fund, Henry Ford)

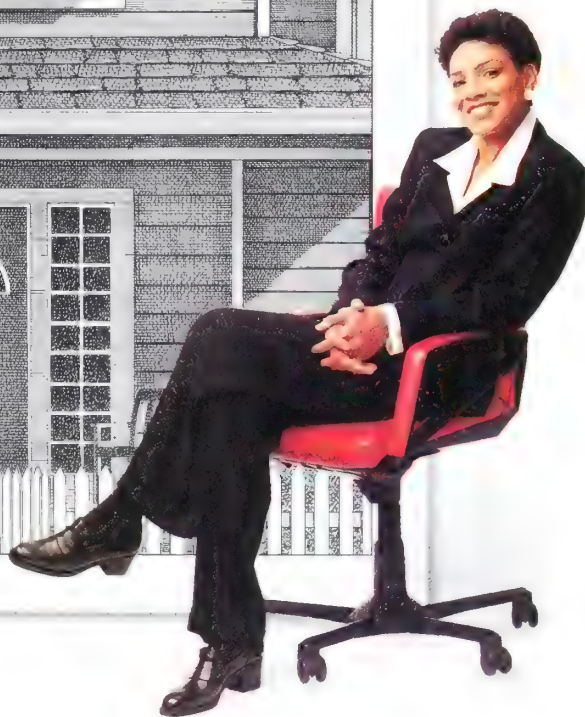


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\$249,000



# The new HP LaserJet 5L printer. Laser is no longer a luxury.

Hewlett-Packard presents the LaserJet for those who thought they couldn't afford one. The HP LaserJet 5L offers your business all the speed, reliability and professionalism you'd expect in an HP LaserJet. Along with one thing you probably wouldn't. A price tag under \$500.

- Crisp, 600-dpi printing
- Four pages-per-minute speed
- No fading or smearing
- No waiting for the first page

- Prints on plain paper, transparencies, envelopes and cards
- Designed for Windows® 95
- Free trial version of QuickBooks 3.1 with purchase before 12/31/95

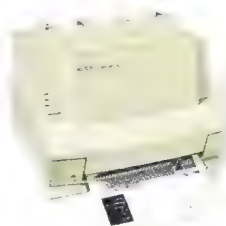
HP LaserJet Printers  
Just what you had in mind.



HEWLETT  
PACKARD

99

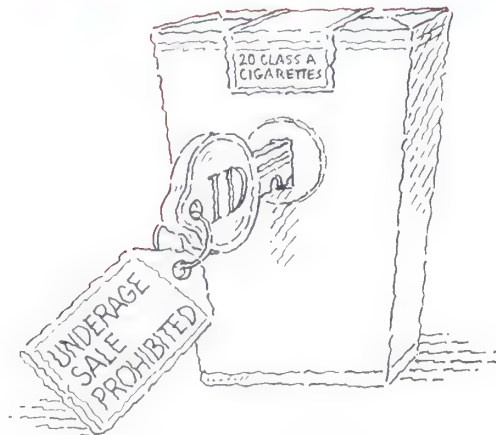
retail price  
may vary.





Our position, word by word.

# No Sale



No one should sell cigarettes to minors. Minors should not have access to cigarettes. They should not smoke. Period.

That's why Philip Morris launched *Action Against Access*, one of the most comprehensive programs ever introduced to combat the issue of youth access to cigarettes.



*Action Against Access* is a voluntary program that is taking some very specific steps.

Here are some highlights: We have stopped the distribution of free sample cigarettes to consumers. We no longer distribute cigarettes through the mail. And we are placing the following notice on all our cigarette brand packs and cartons: "Underage sale prohibited."

In addition, Philip Morris is helping retailers comply with minimum-age laws by providing free signage and funding educational programs.

And, as part of *Action Against Access*, Philip Morris is taking a leadership role in seeking widespread industry and public support for the passage of state legislation designed to prevent minors from having access to cigarettes in vending machines. Additionally, Philip Morris seeks to establish reasonable licensing requirements for cigarette retail sales.

The principle behind *Action Against Access* is simple: The best way to keep kids away from cigarettes is to keep cigarettes away from kids.



PHILIP MORRIS U.S.A.

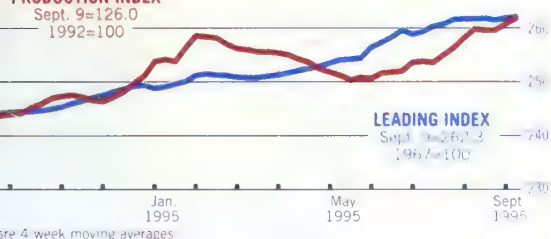
**We want you to know  
where we stand.**

# Business Week Index

## PRODUCTION AND LEADING INDEXES

Change from last week: 0.5%  
Change from last year: 8.1%

### PRODUCTION INDEX



Production index increased during the week ended Sept. 9. Before the four-week moving average, the index slipped to 126.1, from 126.5, as seasonally adjusted output of autos, trucks, and lumber declined in the week.

Leading index edged higher in the latest week. The unaveraged index also slipped, from 267.8, to 267.3. Higher stock prices and slightly lower bond yields offset negative effects of slower growth in materials prices.

Sources: U.S. Commerce Dept., The McGraw-Hill Companies, Bureau of Economic Analysis, Federal Reserve Bank of New York, and others.

## FINANCIAL INDICATORS

|                                   | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|-----------------------------------|-------------|------------|--------------|
| STOCK PRICES (9/16) S&P 500       | 579.23      | 570.58     | 23.3         |
| GOVERNMENT BOND YIELD, Aaa (9/16) | 7.29%       | 7.33%      | -12.4        |
| COMMODITY MATERIALS PRICES (9/16) | 113.0       | 113.5      | NA*          |
| INDUSTRIAL FAILURES (9/8)         | 380         | 332        | 9.8          |
| STATE LOANS (9/6) billions        | \$496.4     | \$495.4    | 11.9         |
| SUPPLY, M2 (9/4) billions         | \$3,714.0   | \$3,709.6r | 3.9          |
| CLAIMS, UNEMPLOYMENT (9/2) thous  | 341         | 348r       | 3.3          |

Sources: Center for International Business Cycle Research (CIBCR), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on failures and real estate loans. \*Historical data available from CIBCR

## INTEREST RATES

|                                     | LATEST WEEK | WEEK AGO | YEAR AGO |
|-------------------------------------|-------------|----------|----------|
| FEDERAL FUNDS (9/19)                | 5.73%       | 5.65%    | 4.73%    |
| DISCOUNT RATE (9/20) 3-month        | 5.69        | 5.72     | 5.07     |
| LIBOR (9/20) 3-month                | 5.69        | 5.71     | 5.08     |
| MORTGAGE (9/15) 30-year             | 7.81        | 7.84     | 8.80     |
| FIXED RATE MORTGAGE (9/15) one-year | 5.90        | 5.85     | 5.68     |
| LIBOR (9/20)                        | 8.75        | 8.75     | 7.75     |

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### CONSUMER CONFIDENCE

Sept. 26, 10 a.m. ▶ The Conference Board's index of consumer confidence stood at 100 in September, down from 101 reading in August. That's the precast of economists surveyed by national, one of The McGraw-Hill Cos. A reading of 100 would indicate consumers are upbeat enough to start spending on an upward track.

### MEETING

Sept. 26 ▶ The Federal Open Market Committee of the Federal Reserve will set monetary policy for the next weeks. The MMS forecast calls for the federal funds rate, now at

5.75%. The steep gains in August retail sales and industrial production justify no change in rates. However, a small quarter-point cut could be warranted under a policy guideline called Taylor's rule, which attempts to balance economic growth and inflation targets. Fed policy under Chairman Alan Greenspan has tracked this rule closely. Also, the inflation-adjusted federal funds rate is high. The Fed cut the federal funds rate by a quarter point on July 6.

### DURABLE GOODS ORDERS

Wednesday, Sept. 27, 8:30 a.m. ▶ New orders for durable goods likely rose 2% in August, reversing their 1.7% drop in July, says the MMS forecast. That's indicated by

the 1.4% increase in the output of durable goods last month. New orders for autos and light trucks likely led the gain, but demand for other products probably increased as well. The backlog of unfilled orders probably gained some ground after posting no change in July.

### NEW-HOME SALES

Friday, Sept. 29, 8:30 a.m. ▶ The MMS survey projects that new single-family homes likely sold at an annual rate of 700,000 in August, down from the 715,000 pace in July. The August decline would be the first drop since April. Still, home sales remain quite solid, thanks to low mortgage rates and good prospects for income growth.

## PRODUCTION INDICATORS

|                                                | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|------------------------------------------------|-------------|-----------|--------------|
| STEEL (9/16) thous. of net tons                | 1,965       | 1,984#    | 12.7         |
| AUTOS (9/16) units                             | 115,881     | 102,705r# | -12.4        |
| TRUCKS (9/16) units                            | 106,209     | 94,668r#  | -11.0        |
| ELECTRIC POWER (9/16) millions of kilowatt-hrs | 64,211      | 66,148#   | 0.6          |
| CRUDE-OIL REFINING (9/16) thous. of bbl./day   | 14,529      | 14,730#   | 3.3          |
| COAL (9/9) thous. of net tons                  | 19,939#     | 20,705    | 4.4          |
| PAPERBOARD (9/9) thous. of tons                | 823.0#      | 846.2r    | -7.9         |
| PAPER (9/9) thous. of tons                     | 839.0#      | 848.0r    | 0.0          |
| LUMBER (9/9) millions of ft.                   | 389.9#      | 457.2     | -2.2         |
| RAIL FREIGHT (9/9) billions of ton-miles       | 23.2#       | 25.7      | 5.9          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WPPA<sup>1</sup>, SFPA<sup>2</sup>, Association of American Railroads

## PRICES

|                                                     | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|-----------------------------------------------------|-------------|----------|--------------|
| GOLD (9/20) \$/troy oz.                             | 384.500     | 384.900  | -1.7         |
| STEEL SCRAP (9/19) #1 heavy, \$/ton                 | 143.50      | 143.50   | 6.7          |
| COPPER (9/15) ¢/lb.                                 | 133.5       | 136.2    | 7.2          |
| ALUMINUM (9/15) ¢/lb.                               | 82.0        | 82.5     | 5.8          |
| COTTON (9/15) strict low middling 1-1/16 in., ¢/lb. | 90.04       | 88.56    | 23.7         |
| OIL (9/19) \$/bbl.                                  | 19.00       | 18.73    | 10.5         |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                        | LATEST WEEK | WEEK AGO | YEAR AGO |
|------------------------|-------------|----------|----------|
| JAPANESE YEN (9/20)    | 103.34      | 102.59   | 97.74    |
| GERMAN MARK (9/20)     | 1.47        | 1.50     | 1.55     |
| BRITISH POUND (9/20)   | 1.55        | 1.55     | 1.58     |
| FRENCH FRANC (9/20)    | 5.07        | 5.15     | 5.28     |
| ITALIAN LIRA (9/20)    | 1617.3      | 1617.0   | 1565.0   |
| CANADIAN DOLLAR (9/20) | 1.36        | 1.35     | 1.34     |
| MEXICAN PESO (9/20)    | 6.300       | 6.285    | 3.408    |

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful



# This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

**BusinessWeek ONLINE**

## Sunday

What happens when personal values clash with corporate beliefs? Talk about this topic with BW Senior Writer John A. Byrne, author of the new book *Informed Consent*. Byrne's book tells the story of John and Colleen Swanson. John shaped the ethics program at Dow Corning Corp., which made the breast implants that Colleen and he came to believe were responsible for destroying her health. **Sept. 24**

**9 p.m. EDT in the Globe**

## Wednesday

The Economy & Election '96: An early look from Standard & Poor's Vice-President and Chief Economist David M. Blitzer, joined by BW's Bill Wolman. **Sept. 27**  
**8 p.m. EDT in the Coliseum**

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

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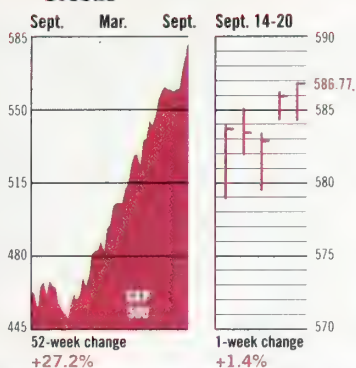


# Investment Figures of the Week

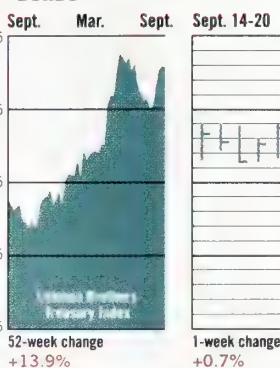
## MARY

ended 4800 on Sept. ed back as investors worry about third- nings reports. High- panies like IBM and warned Wall Street eir profit forecasts gh. But on Sept. 20, ise announcement d voluntarily split hree companies put a happy mood shares shot up \$6 ver 10%. A strong et helped buoy stocks m yields fell below

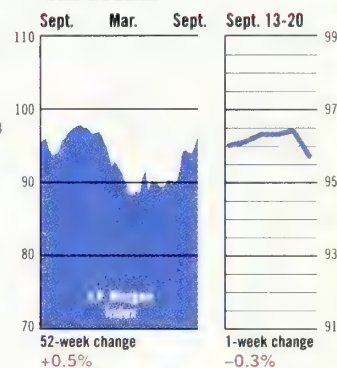
## STOCKS



## BONDS



## THE DOLLAR



## ET ANALYSIS

| KS                         | Latest | % change Week | % change 52-week |
|----------------------------|--------|---------------|------------------|
| INDUSTRIALS                | 4792.7 | 0.6           | 24.4             |
| MPANIES (S&P MidCap Index) | 218.5  | 0.4           | 25.7             |
| MPANIES (Russell 2000)     | 314.8  | -0.4          | 23.7             |
| NIES (Russell 3000)        | 338.2  | 1.2           | 27.3             |

| STOCKS               | Latest   | % change (local currency) Week | % change 52-week |
|----------------------|----------|--------------------------------|------------------|
| MANANCIAL TIMES 100) | 3561.5   | -0.3                           | 18.1             |
| KEI INDEX)           | 18,198.6 | -2.2                           | -8.5             |
| SE COMPOSITE)        | 4550.5   | -0.8                           | 4.4              |

## FUNDAMENTALS

|                              | Latest | Week ago | Year ago |
|------------------------------|--------|----------|----------|
| 90-DAY TREASURY BILL YIELD   | 5.33%  | 5.45%    | 4.91%    |
| 30-YEAR TREASURY BOND YIELD  | 6.47%  | 6.52%    | 7.80%    |
| S&P 500 DIVIDEND YIELD       | 2.32%  | 2.34%    | 2.75%    |
| S&P 500 PRICE/EARNINGS RATIO | 16.9   | 16.7     | 18.3     |

## TECHNICAL INDICATORS

|                                           | Latest | Week ago | Reading  |
|-------------------------------------------|--------|----------|----------|
| S&P 500 200-day moving average            | 515.1  | 511.8    | Positive |
| Stocks above 200-day moving average       | 77.0%  | 78.0%    | Negative |
| Speculative sentiment: Put/call ratio     | 0.61   | 0.53     | Neutral  |
| Insider sentiment: Vickers sell/buy ratio | 2.54   | 2.30     | Negative |

BLOOMBERG FINANCIAL MARKETS

## TRY GROUPS

| TH LEADERS   | % change 1-month | % change 12-month | Strongest stock in group | % change 1-month | % change 12-month | Price |
|--------------|------------------|-------------------|--------------------------|------------------|-------------------|-------|
| URANCE       | 11.8             | 16.0              | PROVIDIAN                | 14.9             | 27.2              | 41½   |
| AND LOANS    | 11.5             | 13.5              | H.F. AHMANSON            | 15.8             | 11.9              | 24¾   |
| AL LOANS     | 11.4             | 46.1              | HOUSEHOLD INTERNATIONAL  | 13.5             | 58.4              | 60    |
| INE INSURERS | 11.0             | 43.4              | AETNA LIFE & CASUALTY    | 12.6             | 46.2              | 70¾   |
| CENTER BANKS | 10.4             | 42.3              | CHASE MANHATTAN          | 14.3             | 69.0              | 60    |

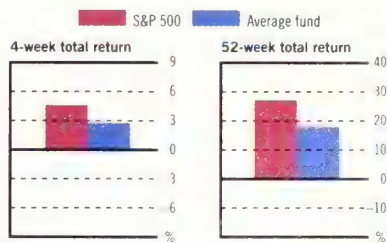
| TH LAGGARDS         | % change 1-month | % change 12-month | Weakest stock in group  | % change 1-month | % change 12-month | Price |
|---------------------|------------------|-------------------|-------------------------|------------------|-------------------|-------|
| ND GLASS CONTAINERS | -9.1             | 4.0               | CROWN CORK & SEAL       | -10.1            | 0.3               | 38¾   |
| ER SYSTEMS          | -7.5             | 40.1              | APPLE COMPUTER          | -18.1            | 3.5               | 36¾   |
|                     | -7.3             | -30.0             | INLAND STEEL INDUSTRIES | -13.1            | -39.9             | 24½   |
| UM                  | -7.2             | 19.1              | ALCAN ALUMINIUM         | -9.1             | 19.4              | 32¾   |
| FIED MACHINERY      | -6.5             | 8.2               | CATERPILLAR             | -13.1            | 4.0               | 58¾   |

## AL FUNDS

| total return            | %    | LAGGARDS                  | Four-week total return | % |
|-------------------------|------|---------------------------|------------------------|---|
| ASIA INFRASTRUCTURE A   | 10.4 | EV MARATHON GREATER INDIA | -6.7                   |   |
| ICKORY                  | 9.8  | PIONEER INDIA A           | -4.4                   |   |
| Y SELECT ENERGY SERVICE | 9.0  | BLANCHARD PRECIOUS METALS | -4.3                   |   |

| total return         | %    | 52-week total return                | %     |
|----------------------|------|-------------------------------------|-------|
| Y SELECT ELECTRONICS | 91.1 | WRIGHT EQUIFUND-MEXICO              | -47.4 |
| SMALLER COMPANIES A  | 87.1 | BT INVESTMENT LATIN AMERICAN EQUITY | -37.6 |
| CAPITAL APPRECIATION | 84.7 | HERCULES LATIN AMERICAN VALUE       | -35.9 |



## VE PORTFOLIOS

unts represent the ue of \$10,000 ne year ago rtfolio

es indicate otal returns

**U.S. stocks**  
\$13,005  
+1.33%

**Treasury bonds**  
\$12,442  
-0.23%

**Foreign stocks**  
\$11,046  
-1.03%

**Money market fund**  
\$10,541  
+0.12%

**Gold**  
\$9,840  
+0.46%

is page are as of market close Wednesday, Sept. 20, 1995, unless otherwise indicat- groups include S&P 500 companies only; performance and share prices are as of mar-

ket close Sept. 19. Mutual fund returns are as of Sept. 15. Relative portfolios are valued as of Sept. 19. A more detailed explanation of this page is available on request. r=revised NA=Not available



# THE STORY YOU SHOULD BE READING

We are not accustomed to writing about ourselves, but an urgent issue has arisen that warrants comment. On Sept. 13, The McGraw-Hill Companies, publisher of BUSINESS WEEK, received a fax from the U.S. District Court for the Southern District of Ohio barring us from publishing an article. This was the first time in our 66-year history that we have ever been forced by the government to pull a story. This action is a most egregious attempt to curtail the free flow of information essential not only for intelligent political discourse but also for rational economic decision-making.

The story involved Procter & Gamble Co.'s \$195 million suit against Bankers Trust Co. over its sale of derivatives to P&G. The prior restraint order was imposed on BUSINESS WEEK without notice by a judge who appears to have received *ex parte* communication on the phone from attorneys involved in the litigation. No briefs were filed, and BUSINESS WEEK was given no opportunity to be heard by the court, which faxed the restraining order just three hours before the publication deadline.

The basic legal issue is prior restraint—a lawyer's way of saying government censorship. We believe the gag constitutes a serious violation of the magazine's rights under the First Amendment. It prevents us from fulfilling our mission of providing all pertinent information on national and global business and economic affairs necessary for readers to act as productive and free citizens of this nation. The ability to report is at the core of the protections afforded by the First Amendment. And for good reason. The efficient workings of America's political and economic systems depend on the unfettered ability of the press to report on the news in a timely fashion.

## A DANGEROUS PRECEDENT

The power to censor is the power to regulate information. It is unacceptable in a market democracy. Fortunately, legal precedent overwhelmingly favors the right of free speech over virtually any other issue. No prior restraint on the publication of information has ever been upheld by the Supreme Court. The judicial system has long held that "prior restraints on speech and publication are the most serious and least tolerable infringements on First Amendment rights" (*Nebraska Press Assn. v. Stuart*, 1976). The courts have clearly established that only in the case of war and national security can the principle of free speech possibly be superseded. Even then, the hurdle of proof is extremely high. In the Pentagon Papers case in 1971, the High Court rejected efforts to impose prior restraint despite the government's arguments that national security was at stake and the documents had been stolen.

BUSINESS WEEK, of course, is not above the law, and we are obeying the injunction while appealing it. We have moved to stay the order before the Supreme Court. The process of appeal, unfortunately, takes a great deal of time and the article goes unpublished and unread by millions of readers.

The banned story contains information from documents presented during the discovery process that both parties and

the court agreed were to be sealed and kept from the eye. The district court argues that in imposing prior restraint on BUSINESS WEEK, it is preserving the sanctity of the system by protecting the privacy of that discovery process.

## AT STAKE: YOUR RIGHT TO KNOW

The federal judiciary must have the right to set and enforce rules. Since a modicum of privacy is essential to the negotiation process and integral to the judicial system, we recognize the interests of the judiciary and the media are sometimes in conflict. But blanket seals routinely given are not the answer. Moreover, BUSINESS WEEK broke no judicial rules. The magazine is not a party to the litigation, nor is it a party to the process of sealing the documents. Indeed, the order specifies it is only between P&G and Bankers Trust.

The fact is, BUSINESS WEEK lawfully obtained a copy of the documents. On Sept. 1, 1995, P&G motioned to amend its original complaint against Bankers Trust. That motion included new, more serious racketeering charges. It was not filed under seal, nor did the motion itself indicate that documents attached to it were filed under seal. When the magazine, following the most useful journalistic practice, contacted Bankers Trust and P&G for comment, the litigants refused to comment and persuaded the district court to gag BUSINESS WEEK.

The prior restraint placed on BUSINESS WEEK is the manifestation of a trend to seal documents in civil cases to keep information from public view. In this case, the litigants are giant, publicly traded corporations. The information obtained from P&G about Bankers Trust's sale of derivatives that is now secret could have serious consequences for dozens of companies and millions of shareholders. Many institutions are still invested in derivatives to pension funds, corporations, and institutional money managers. They have a right to know how Bankers Trust operated with its clients and why it is trying so hard to keep this information secret. If it were up to BUSINESS WEEK, the business and financial communities would already know.

It is not fashionable in these times to support the media, but the stakes in this constitutional case are extremely high. That is why so many members of the print and electronic media, including rivals—back BUSINESS WEEK, Dow Jones, The New York Times, Bloomberg, Time, Newsweek, ABC News, America Publishing, Advance Magazine Communications, the Satellite Information Network, the Magazine Publishers Association, and the Association of American Publishers have filed in court as *amici curiae* in support of BUSINESS WEEK. In their statement, they say banning the article "would allow parties involved in highly publicized legal proceedings to dictate what the press can and cannot print and televise, and what the public can and cannot know."

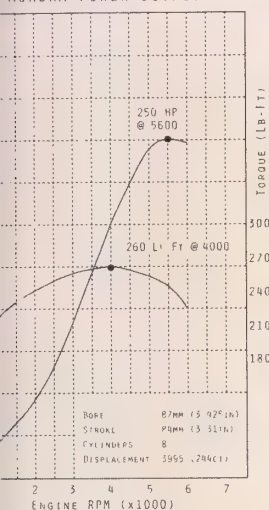
This is intolerable in a free society. BUSINESS WEEK, of course, is legally responsible for all that it publishes. But prior restraint is a totalitarian act. That's why prior restraint is unconstitutional and a danger to us all.



OMOBILE COMPANIES TALK ABOUT HOW FAST  
R CARS ARE FROM 0-60. WHEN'S THE LAST  
YOU PASSED A CAR STARTING FROM 0?



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A USER-FRIENDLY GAS PEDAL

happy acceleration off the  
a worthy trait for an  
mobile to have. Yet, the  
is most driving situations  
st the legal kind) require  
underway to have deep  
es of passing power. That  
of ability is measured  
eque. It's what makes  
around a trailer truck on  
lane road a joy, rather than  
iac event. And torque is  
ing the Aurora™ has  
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SS WEEK  
OCTOBER 9

# BusinessWeek

ER 9, 1995

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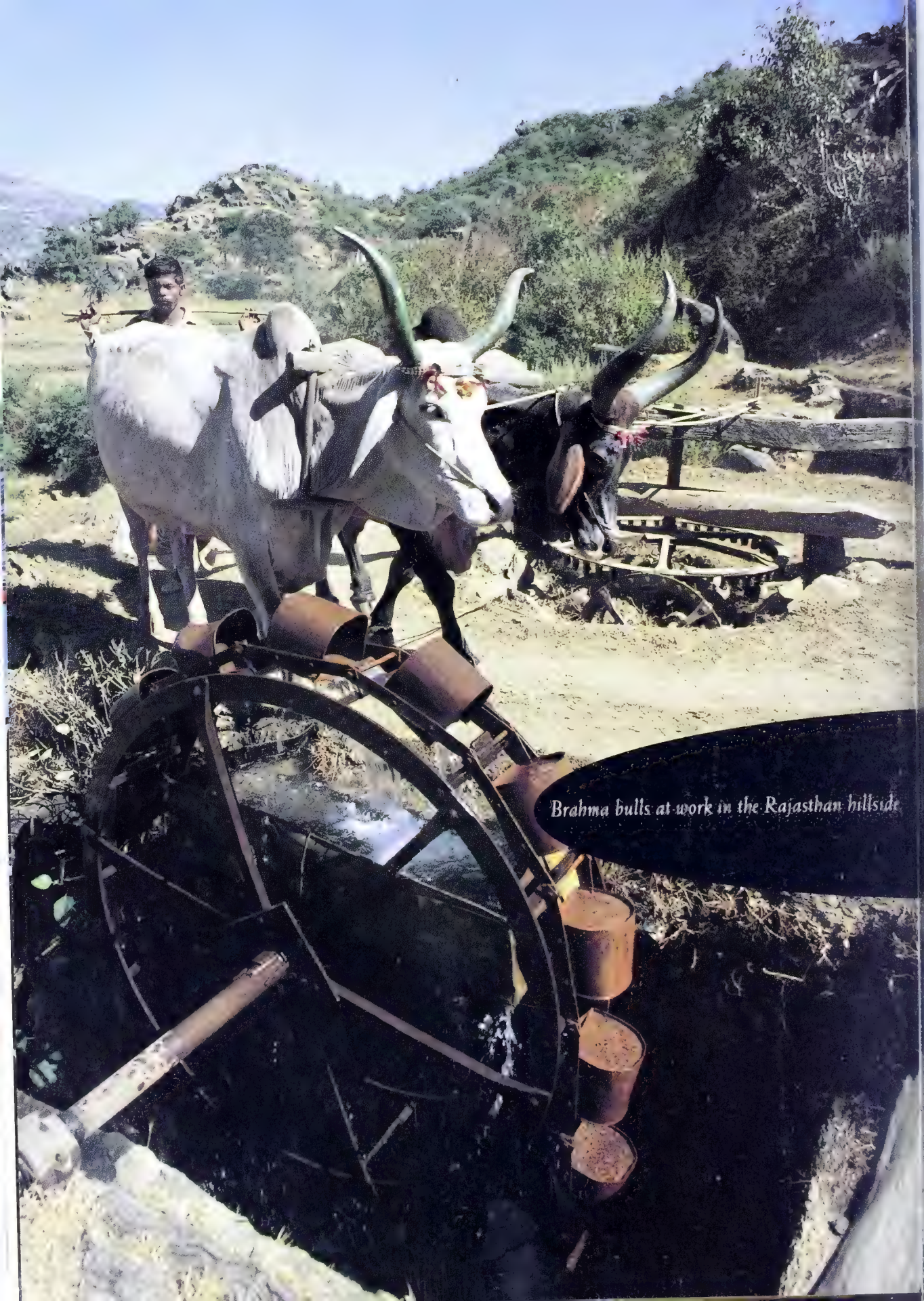
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# Up Front

EDITED BY STEPHEN BAKER, WITH OLUWABUNMI SHABI

## EXECUTIVE SUITE

### PEROT BAGS A BIG BLUE PRIZE

ROSS PEROT HAS LANDED A high-profile industry executive for his seven-year-old computer consulting business, Perot Systems. James Cannavino, former top strategist at IBM, is to be named president at Perot's Dallas-based company on Oct. 2, say sources close to the billionaire.

Cannavino, 51, will run day-to-day operations as president and COO, while Perot's old buddy Morton Meyerson, the company's chairman and CEO, will focus increasingly on the big picture.

The timing looks propitious for Cannavino. As recently as

two years ago, Perot Systems was getting whipped by Cannavino's IBM and Perot's old company, EDS. But now the company appears to be back on track. In early September, Swiss Bank Corp. took a 24.5% stake in it in return for the bank's \$250 million a year in business. That gives Perot Systems a foothold in the global financial



**CANNAVINO:** Ross's find

services business. And Cannavino's arrival positions the company for an IPO, probably in early 1997. Perot, who owns 20%, could—once again—cash in big, as could

Cannavino, who was wooed with stock options.

Cannavino left in March due to an illness in his family. At the time, he declined to sign a noncompete agreement, which cost him millions in options at Big Blue.

Meanwhile, IBM named J. Bruce Harreld, former president of Boston Chicken, to fill the empty chief strategy post.

*Mark Lewyn*

## THE HUSTINGS

### CAMPAIGN '96: A BETTOR LOOK



**GRAMM:** 6 to 1, says Ladbrokes

EVEN WITHOUT DECLARING his candidacy, Colin Powell has swept ahead of all challengers for the Presidency. At least that's the word from the Ladbroke Group, the famed bookmakers based in London. As Powell stomps the country on his book tour, global gamblers are betting on him in record numbers for a preelection year, say the bookmakers.

Ladbrokes gives Powell 2:1 odds to capture the White House in '96, compared with 7:2 for Senator Bob Dole. Before Powell's book tour, Dole had 2:1 odds,

while Powell was a 25:1 long shot.

President Clinton is still the favorite, with 7:4 reelection odds. And other challengers? Texas Senator Phil Gramm, 6:1; California Governor Pete Wilson, 10:1; House Speaker Newt Gingrich, 14:1; Former Education Secretary Lamar Alexander

It has been the worst hurricane year on record. But for all the tragedy, 1995's storms haven't cost insurers much; not one hurricane dents the top ten. Why? While pummeling the Caribbean, the 'canes



**AFTER ANDREW**

have largely spared the more heavily insured U.S. mainland. These days, as Andrew proved in 1992, hurricanes hitting the U.S. wreak billions in damages much faster. The reason:

and Vice President Al Gore, 33:1; commentator Pat Buchanan, 100:1; and publisher Malcolm Forbes Jr., 200:1.

Dark horses shouldn't despair too much, however. In the fall of 1991, Ladbrokes rated Arkansas Governor Clinton an 8:1 underdog. And President Bush was an odds-on favorite. *Rick Dunham*

## THE LIST STORMY WEATHER

Sunbelt migration has fed heavy, often flimsy construction in 'cane country.

### WORST HURRICANES OF THE LAST 30 YEARS

| Year | Name     | Insurance loss* |
|------|----------|-----------------|
| 1992 | ANDREW   | \$16,508        |
| 1992 | INIKI    | 1,693           |
| 1991 | BOB      | 675             |
| 1989 | HUGO     | 4,953           |
| 1985 | ELENA    | 736             |
| 1985 | GLORIA   | 568             |
| 1983 | ALICIA   | 991             |
| 1979 | FREDERIC | 1,469           |
| 1970 | CELIA    | 1,127           |
| 1965 | BETSY    | 2,320           |

\* Estimates in millions of 1995 dollars

DATA: INSURANCE INFORMATION INSTITUTE, BUSINESS WEEK

## VIVA LAS VEGAS

### HIT ME. NO, I MEAN WITH A CARD

WHO SAYS THE HOUSE ALWAYS wins in Vegas? The Grand and the Hilton Vegas came up big losses few months back when a Australian media mogul Ken Packer walked off with an estimated \$20 million after a hot weekend at the blackjack tables. Packer, who is known to wager as much as \$250,000 a hand and to dish out \$100,000 a night in tips, contributed mightily to the \$6.6 million second-quarter loss this year.

It didn't take long for many of the casinos to roll up the red carpet for Packer, denying him the usual complimentary digs and drinks—"comping," in Vegas jargon. The casinos complain that Packer routinely shoos the players from the blackjack pits so that he could play several tables at a time. Worse, he developed a reputation for running out with his winnings, instead of settling up to give some of them back. "The object of comping someone is that he's going to play with you for a while, not take your chips and bolt," says a gambling exec. Packer, who roams from casino to casino, "doesn't seem to play by those rules."

Maybe, but Packer, majority owner of Australia's In Network, isn't likely to be a pariah in Las Vegas for the Hilton, which refuses to comment about its customer. Packer said to be playing to Packer again. Not so at the Grand, however, which still refuses to talk about its customers. Other casinos are also keeping quiet—as is Packer.



**PACKER:** millions

*Ron Green*





Grand Marnier, slightly less mysterious than love.



# Up Front



**TEST AISLE:** Who is helping whom?

for mistakes and cheating. Bloopers trigger an alarm that alerts clerks nearby, who also card youthful customers for tobacco or alcohol.

Folks don't save any money by playing cashier, but they could

save time. Kroger says up to 42% of the sales at its Columbus test store are do-it-yourself.

The new system costs \$30,000 per aisle. Kroger claims that no workers will lose jobs to this automation, saying that clerks will keep busy with additional labeling. The United Food & Commercial Workers, however, denounce the do-it-yourself concept as a "job-cutting, cost-cutting mechanism, with no advantage for the customer." The union's Greg Denier suggests that "maybe if customers come early, they can unload the truck and stock the shelves." *Scott LaFee*

## AUTOMATION BLUES

### YOUR NEXT JOB: CHECKOUT CLERK

SELF-SERVICE CHECKOUT IS coming. Three big supermarket chains—Kroger, Price Chopper, and Finast—are experimenting with a system that lets customers scan their own groceries, bag them, and pay automatically with a credit card.

At a Columbus (Ohio) test store for Cincinnati-based Kroger, a customer scans the items, then puts them on a conveyor belt that passes under an infrared arch to check

## PRODUCT PEEK

### HEY, WAKE UP AND SMELL THE HOPS



COFFEE-FLAVORED beer? That may not be your cup of joe, but Starbucks has teamed up with a brewery to produce just such a dark, heavy beer with a creamy head. For now, Double Black Stout sells only in the Northwest, on tap in Seattle and Portland brew pubs. Redhook Ale Brewery and Starbucks will start shipping 22-ounce bottles of the concoction (cost: \$3) to grocery stores on Oct. 1. The label will read "Brewed

with Starbucks Coffee."

The idea came from Sanford Monblat, Redhook's vice-president for sales, who felt the U.S. market was lacking in stout, a beer whose heavy flavor seems to taste of coffee. Redhook goes a step further by adding a shot of coffee extract during the brewing process.

Double Black Stout certainly gives a person a double buzz, with as much caffeine as a cup of black tea and 6% alcohol content. Redhook (25% owned by Anheuser-Busch) might start distributing the product around the country next year if it takes hold in the trend-setting Northwest. *Seanna Browder*

## DRAWN & QUARTERED

"SOMETHING TELLS ME WE'RE BEGINNING TO RUN OUT OF IDEAS...."



## CAREER PATHS

### THESE DAYS, THOSE WHO CAN, CONSULT

CONSULTING FIRMS ARE scooping up greater numbers of MBAs from the nation's elite B-schools. A record 32% of the Class of 1995 from 19 top-tier business schools rushed off to consulting, up from 23% last year, says Brecker & Merryman. What's more, the New York-based personnel consultants say the numbers will keep climbing.

The chief appeal for MBA grads is—let's face it—the princely pay, which helps with the mountains of debt accumulated in B-school. Brecker

& Merryman says consulting firms outpace other employers by paying \$70,000 on average. That's not including generous signing bonuses or other incentives. And, sure: Consulting is good preparation for big corporate jobs later on. (Example: McKinsey & Co., CEO of IBM.)

### MBA Grads Entering Consulting

|                        | 1994 | 1995 |
|------------------------|------|------|
| MIT (SLOAN)            | 32%  | 46%  |
| DARTMOUTH (TUCK)       | 27   | 39   |
| HARVARD                | 32   | 38   |
| NORTHWESTERN (KELLOGG) | 27   | 38   |
| PENN (WHARTON)         | 24   | 28   |

DATA: BRECKER & MERRYMAN INC.

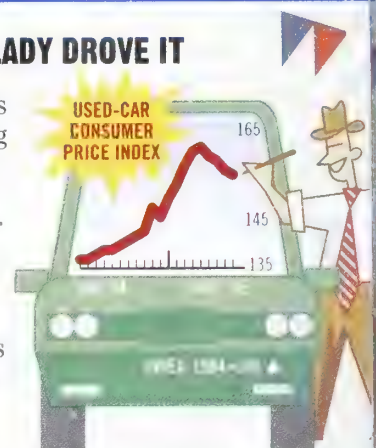
Jobs plentiful in consulting industry, which has grown tremendously recently thanks largely to corporate America's tendency to restructure without hiring in-house strategists. Opening at investment banks, a magnet for newly minted MBAs in the 1980s, are laid down. *Lori Bongiorno*

## THE BIG PICTURE

### A LITTLE OLD LADY DROVE IT

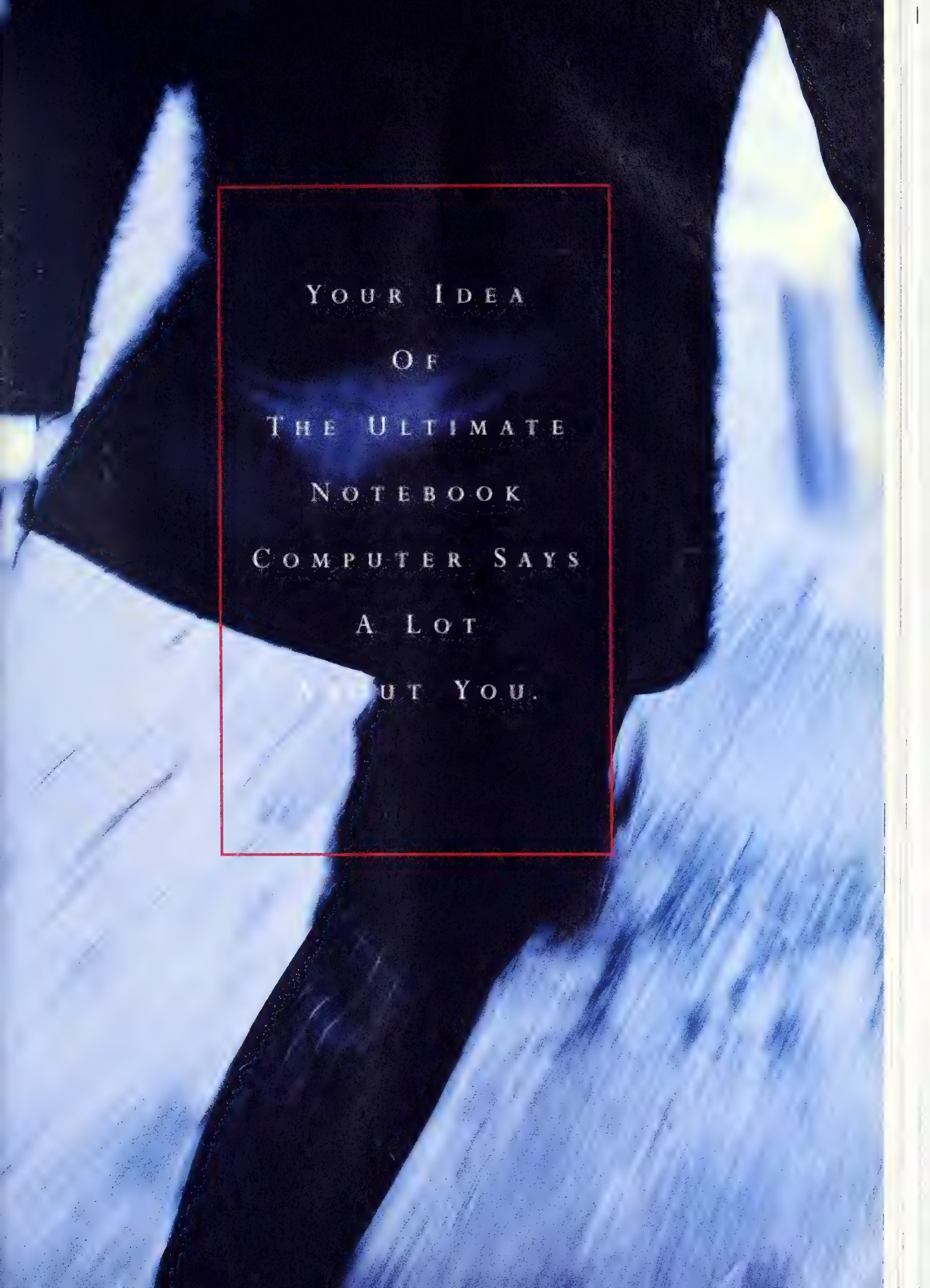
Prices for used cars have been dropping since spring. Why? Edward Yardeni, chief economist for C.J. Lawrence, believes dealers must sell a sudden abundance of autos whose leases have expired.

DATA: C.J. LAWRENCE INC.



**FOOTNOTES** Projected 1996 pay hikes in computer and software industries: **4.6%**; in aerospace: **3.7%**



The background is a dark, textured surface, possibly a book cover or a piece of fabric, with a prominent red rectangular border. The text is centered within this border in a white, serif, all-caps font. The text is arranged in seven lines, with the first line being the largest and the last line being the smallest. The overall effect is one of mystery and intrigue.

YOUR IDEA  
OF  
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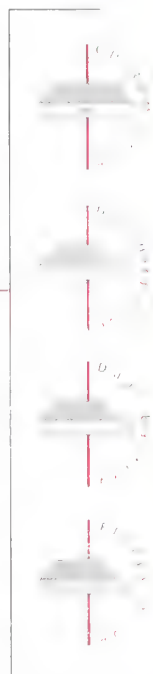
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## MANAGEMENT MECCAS: PILGRIMAGE IS NO PANACEA

I want to share a few comments regarding your article "Management meccas" (Cover Story, Sept. 18). The problem with these "tours" is that people assume that simply by visiting a company suspected of best practices, somehow those best practices will transfer to the visitor. Much of what is happening today in the name of benchmarking is really just industrial tourism.

Moreover, the total costs of these "tours" and benchmarking site visits are far from inexpensive, as are the costs of implementation. Before you spend the money, do your homework and know what it is that you are looking to improve.

Margaret Orth  
 Benchmarking Program Developer  
 L. L. Bean Inc.  
 Freeport, Me.

It is amazing the way some executives think. They spend their time and money watching a "show" by so-called successful organizations. Have they ever thought about how these "successful" companies became successful? Certainly not by imitating other companies. Just by watching a production of an opera one does not become another Verdi.

Jack Asgar  
 President  
 Practical Management Inc.  
 Las Vegas

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Gary S. Altman  
 Pak Mail  
 Colorado Springs, Colo.

## EX-IM BANK BANKROLLS SMALL BUSINESSES, TOO

It was dismaying to read your article "GOP magic: Trimmed budget, brimful trough" (Government, Sept. 4), which said "the Export-Import Bank shows largesse on big U.S. corporations, does little for the country's small- and midsize companies."

Ex-Im Bank has sharpened its eyes for assistance for smaller companies since 1993. The result: More than 70% of the transactions authorized by Ex-Im Bank were dedicated to small business last year. Also, 15% to 20% of export volume is for small-business transactions.

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Kenneth D. Bland  
 President and Chairman  
 Export-Import Bank  
 Washington, D.C.

## PUTTING ECONOMIC NATIONALISM TO THE TEST

Your article "Economic Nationalism: Disaster ahead" (Editorials, Sept. 18) correctly identifies the problem: As globalization expands, workers in the industrialized countries see their jobs lost and their incomes erode. "Improving the skills of the U.S. workforce" is essential, but in no way sufficient, step toward mitigating the negative impact of free trade and mobile capital.

A truly long-term solution would involve rewriting the rules of international commerce to remove some of the perverse incentives that currently reward footloose corporations. If we work in international arenas toward agreed-upon minimum labor and environmental standards, corporations will have less leeway to bargain down workers' wages. Maybe then governments will compete to attract capital by offering the most skilled workforce and the best infrastructure rather than the

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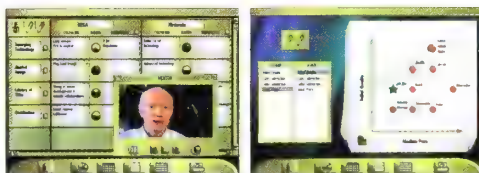
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| Ashtor Binkley    |             |              |

Buttons: Ok, Remove, Remove All

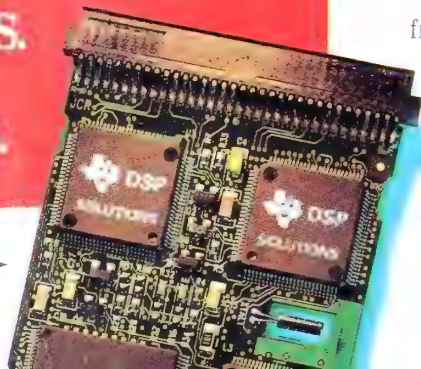
T I D S P S O L U T I O N S

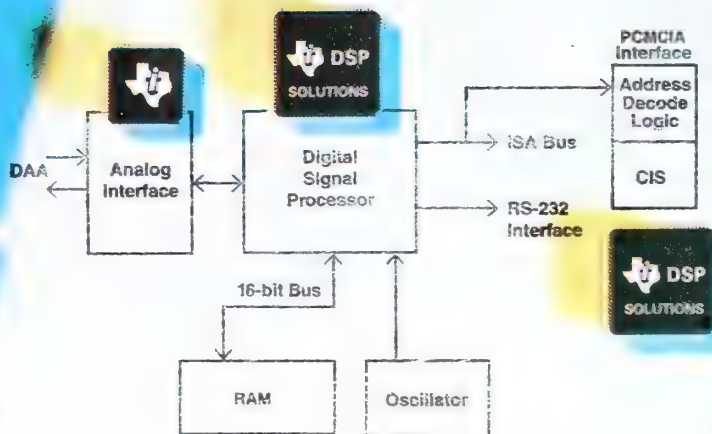
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## MY AMERICAN JOURNEY

By Colin L. Powell with Joseph E. Persico  
Random House • 643pp • \$25.95

# A GREAT AMERICAN TALE— BUT WHAT'S THE ENDING?

Colin L. Powell's autobiography, *My American Journey*, should come with a warning label: Readers expecting a political manifesto from their favorite fantasy Presidential candidate will be sorely disappointed.

Not that *American Journey* isn't a great read. But the book's strength lies not so much in Powell's musings about politics and the country's future as in his recalling a life that is, at once, recognizable to most Americans and yet extraordinary in its scope and texture. It's like the story of a shrewd Forrest Gump—in its style, it evokes *The Autobiography of Benjamin Franklin*.

Oh, Powell is keeping his Presidential options open, all right. And after 600-plus pages of his journey from the South Bronx to the White House, where he served as National Security Adviser and later counseled two Presidents as chairman of the Joint Chiefs of Staff, you'll wish him the best. Powell's life truly offers a fresh embodiment of the American dream. The fact that he is of Jamaican descent, just an average goof-off of a kid whose parents earned a daily wage in New York's garment industry, makes the saga doubly poignant. In today's harsh, winner-take-all society, the account offers hope to adults who tremble as they contemplate the future of their own unremarkable kids.

What Powell found—really just fell into as a teenager—was the Army, an institution that “made sure that performance would be the only measure of advancement,” the 58-year-old former-general writes. It's a statement that could be read as an indictment of a free-enterprise system that offers less of a meritocracy than the military. But Powell could hardly be considered a social rebel, or even a supporter of racial preferences: “Affirmative action in the best sense promotes equal consideration, not reverse discrimination,” he

says, adding, “all discrimination is offensive.”

The book is built upon such common-sense pronouncements, “Powellisms” if you will. Every story told here—from Powell's tours of duty in Vietnam and Korea to his career as a defense adviser during the Carter and Reagan Administrations to his managing the Persian Gulf War for President Bush—is punctuated with life's lessons learned. Some examples: Never step on enthusiasm; you never know what you can get away with until you try; hand the boss a solution instead of a can of worms.

Standing alone, such aphorisms sound as though they were lifted from *Reader's Digest*. Set against Powell's experiences—the horror of watching a fellow soldier die in Vietnam or the pain of hearing the white owners of a Deep South hamburger joint cackle after denying him service—the tenets take on a special resonance. Another Powell life lesson: Get mad, then get over it. “Nothing that happened off post, none of the indignities, none of the injustices, was going to inhibit my performance.... I felt anger; but most of all I felt challenged. I'll show you!”

When, through the force of his intelligence, personality, and skills, he is chosen to be Ronald Reagan's top national security aide, Powell proudly observes: “National Security Advisers to Presidents are not chosen as tokens. The job is real, demanding, and critical.” But Powell never loses the common touch. A lover of West Indian music as well as *The Music Man*, he recalls how he gushed over meeting Sergeant Elvis Presley in Germany in the '50s.

Most of the book's news nuggets have already been picked over by the media: He condemns the sales of arms to Iranian hostages under President Reagan as “wrong” and disparages the lie Horton ads used by President Bush in the 1988 election as offensive. He says he was appalled by the ad hoc decision-making in the Clinton White House. Looking ahead to a possible political career, he notes that “neither the two major parties fits me comfortably in its present state.” And he says, “I distrust rigid ideology from any direction, and I am discovering that many Americans feel just as I do.”

When Powell finally does get to his political manifesto in an epilogue, it's a letdown. After 609 pages of a wonderful American story, Powell's vision of a “new order... defined by trade relations, the flow of information, capital, technology, and goods, rather than by armed glaring at each other across borders sounds like what every other contemporary politician is muttering. The general himself has a phrase for such muttering, drawn from experiences with excessive military formality: “breaking the starch.” It diminishes the rest of the work, and prompts the question: Should Powell risk tarnishing a life of such accomplishment and character by the petty rough-and-tumble of American politics?

A month ago, I was coming into work in Washington on the Georgetown Parkway. On the radio, a commentator was droning on about the possibility of a Powell candidacy. I looked to my left in backed-up traffic and there he was, the general at the center of a modern-day media blitz alone in a late-model Mazda, driving himself into town. It shocked me at the time. Now, after having read his book, it seems perfectly fitting. Had I known then what I know now, I would have rolled down the window and yelled, “Don't do it, general. It's just not you. You've already given the country a career of service.”

BY DOUGLAS HARBRECHT

Harbrecht is News Editor of *BUSINESS WEEK's* Washington bureau.



**COLIN POWELL**  
with Joseph E. Persico

## WHEN POWELL FINALLY DOES GET TO HIS POLITICAL MANIFESTO, IT'S A BIT OF A LETDOWN



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BY STEPHEN H. WILDSTROM

## CAN SOFTWARE HELP MEMORY?

**W**indows 95 has a voracious appetite for memory. Microsoft's official minimum requirement of four megabytes of RAM will give you a machine too slow for anything more taxing than playing solitaire. Even 8 MB, the quantity of memory installed in most machines being sold today, can be painfully sluggish when running heavy-duty programs such as Microsoft Office.

Nothing, not even a faster processor, will do as much to improve performance as an extra 4 or 8 MB of RAM. But soaring demand has kept memory-chip prices high, and a 4 MB module will set you back about \$170—more if you need professional help installing it. Small wonder that software that promises to improve performance at a fraction of the cost of chips has great appeal. Indeed, software that does just that for the old Windows 3.1 has been quite popular.

**"SMALL BENEFITS."** Unfortunately, it seems there's no cheap lunch when it comes to Win95 memory. SoftrAM 95 from Synchronys Softcorp (310 842-9203) is an update promising that "4 MB becomes 8 MB. 8 MB becomes 16 MB. You become doubly productive." But both my casual tests and more formal benchmarking by National Software Testing Labs (like *BUSINESS WEEK*, a part of The McGraw-Hill Companies), found that the \$35 SoftrAM 95 had little effect on performance.

NSTL ran Win95 machines through a variety of memory-intensive tests with and without SoftrAM. One test, on which SoftrAM produced its best showing, prepared for printing a complex Microsoft Word document that included PowerPoint slides and data from an Excel spreadsheet. On a Gateway 2000 Inc. computer with a 66-megahertz 486 processor and 4 MB of RAM, the job took a hair under 12 minutes. Using Soft

Poertner admits, though he adds: "In some cases, we can get four or five times the amount of actual RAM."

Poertner says some tests might show poor performance because "you will see the effect only when you have exhausted physical RAM." But when I more than filled up the memory of both 8 MB and 16 MB machines by opening multiple copies of Word, I still found little improvement with SoftrAM.

**BEST-SELLERS.** One obvious source of RAM boosters' appeal is that similar products, including a previous version of SoftrAM, RAM Doubler from Connectix, and MagnaRAM from Quarterdeck, could

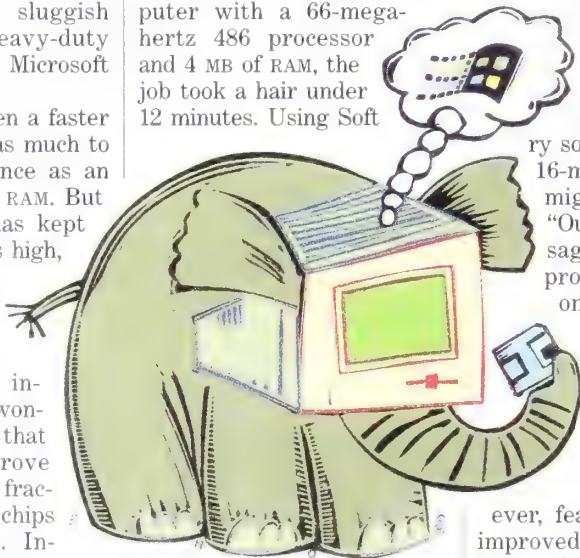
produce significant performance gains under Windows 3.1 and DOS. The programs used memory so poorly that even a 16-megabyte computer might generate an "Out of Memory" message with just a few programs loaded at once. In recent months, memory boosters have consistently been near the top of *PC Magazine's* software best-seller list. Windows 95, how-

ever, features dramatically improved memory management, which takes full advantage of all the RAM you have installed. And Win95 is far more efficient in its use of virtual memory. As a result, it's much harder for add-on software to yield big improvements.

Eventually, programmers will find ways to improve Win95 memory use. Both Quarterdeck and Connectix are readying Win95 versions of their memory software. Synchronys is also working on enhancing SoftrAM. But for now, at least, it appears that if you want the improved Win95 performance that extra memory brings, you'll have to buy chips.

RAM cut just 15 seconds off the task. Adding 4 MB of memory chips saved nearly 9% minutes.

All versions of Windows work by swapping programs and data between RAM and the hard drive, a method that's called "virtual memory." Rainer Poertner, president of Culver City (Calif.)-based Synchronys, says SoftrAM works both by compressing data to fit more into RAM and by replacing the Microsoft software that controls virtual memory with more efficient programming. "There are a few cases where you'll see rather small benefits,"



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ping technology, the Metriplex network sends out bond futures, and currency market quotes, along with financial news from Knight-Ridder. Data can be analyzed on the 200LX's built-in Lotus 1-2-3 software. The DataPulse II costs \$995, plus service beginning at \$125 a month. A version lacking the analytical capabilities runs on a \$295 Motorola pager, while a product for a Digital Equipment laptop is under development.

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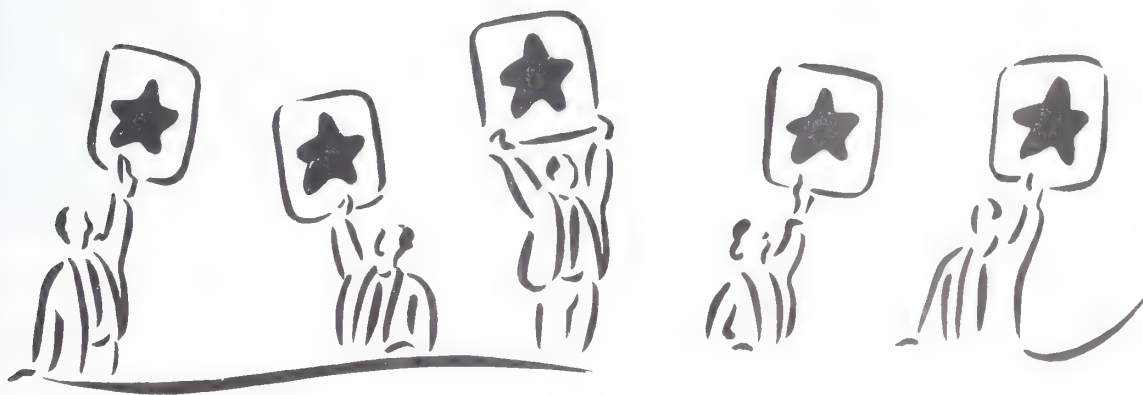
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\*\*Past performance is no guarantee of future results. Performance figures cited are historical and include changes in share price and reinvestment of dividends and capital gains, which will fluctuate so that shares, when redeemed, may be worth more or less than their original cost.

†Source: Lipper Analytical Services, Inc.

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BY PAUL CRAIG ROBERTS

# SUPPLY-SIDE HAS THE ANSWERS TO GLOBAL PRESSURES, TOO



**ACT II:**  
American workers need help—but protectionism won't do the trick. Better to cut taxes on capital, which would boost investment

There hasn't been a macroeconomic policy debate for so long that it is hard to remember what they were like. The Keynesian demand-management edifice has crumbled, just like the Berlin Wall and Soviet communism. Today, fiscal policy is entirely dominated by the supply-side emphasis on the relative price, or incentive, effects of taxation, and we no longer hear about how "expansionary fiscal policy" (budget deficits) make it impossible for the Federal Reserve to control inflation.

For almost 15 years, the U.S. has enjoyed high employment and low inflation—an impossible combination, according to the conventional wisdom in 1980. The Fed no longer takes the economy on wild roller-coaster rides, juicing up economic activity with monetary expansion and then jamming on the brakes to fight the resulting inflation. Supply-side economists have been proven right that the "Phillips curve" trade-off between employment and inflation was a correctable consequence of mixing easy money with bad incentives.

Today, all tax reform proposals—the consumed income tax of Senators Sam Nunn (D-Ga.) and Pete V. Domenici (R-N.M.), the flat-rate tax of Representative Richard K. Armey (R-Tex.), and House Ways & Means Chairman Bill Archer's (R-Tex.) suggestion to replace the income tax with a national sales tax—stress reducing the impact of taxation on the cost of labor and capital. No one any longer regards tax policy as a tool for altering disposable income and aggregate demand.

In retrospect, Keynesian economics was the handmaiden of Big Government. As the era of government-run economies comes to a close, new issues will arise from the competitive pressures of global capitalism. Right now, Presidential candidate Pat Buchanan might have his hands on one of them.

**INEFFICIENT TAX SYSTEM.** There is evidence that lower-skilled workers in the U.S. are faring less well in international competition than higher-skilled ones. An explanation could be that higher skills are rarer in the world economy than lower skills; therefore, free trade hurts lower-skilled workers in high-wage economies.

In Europe, where wages are protected, global competitive pressures are forcing up the unemployment rate, which has risen from half the U.S. rate in the past to twice the U.S. rate today. In the U.S., with its more

open labor market, employment of low-skilled workers has remained high, and the adjustment is taking place in real wages.

Buchanan wants to respond to this perceived problem with trade protection, which carries risks and costs of its own. A much better way to respond to global competition would be to reduce the tax component in the cost of U.S. output. If capital were not subject to multiple layers of taxation, there would be more capital investment and U.S. workers would have higher productivity.

Similarly, if Social Security were privatized, the payroll tax could be terminated, thus reducing the cost of U.S. labor. A more productive and less costly labor force will fare better in international competition.

The advantage of free trade is that it enforces the supply-side emphasis on reforming an inefficient tax system and shifts the discussion away from old distributional arguments to the competitive benefit to U.S. workers. Global competition makes it even more obvious that attempts to shift the domestic tax burden from labor to capital reduces the earnings of labor.

**LABOR MILLSTONE.** Trade protection is the wrong answer. It would provide a false sense of security and impede the restructuring of U.S. economic policy that is necessary for the U.S. to remain a global competitor.

The competitive pressure on lower-skilled labor means that journalist Peter Brimelow also has his hands on a hot issue with his book about immigration, *Alien Nation*. Whatever the *de jure* state of our immigration policy, in practice it seems to be open borders. Brimelow says that the vast majority of the immigrants pouring in to the country are unskilled; thus, the U.S. is accumulating a labor force destined to do less well in global competition.

The increasing proportion of unskilled labor will add to the growing disparity between the incomes of high-skilled and low-skilled workers. This will facilitate the efforts of free-wing economists to shift the economic policy discussion back to distributional issues away from the reforms necessary to maintain an open economy.

Sooner or later, the economics profession will recover from the shock of losing the macro debate to "voodoo economists" and realize that the answer to the global challenge lies on the supply side.

Paul Craig Roberts is John M. Olin Fellow of the Institute for Political Economy and Distinguished Fellow of the Cato Institute in Washington, D.C.



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adapt to meet and neutral-  
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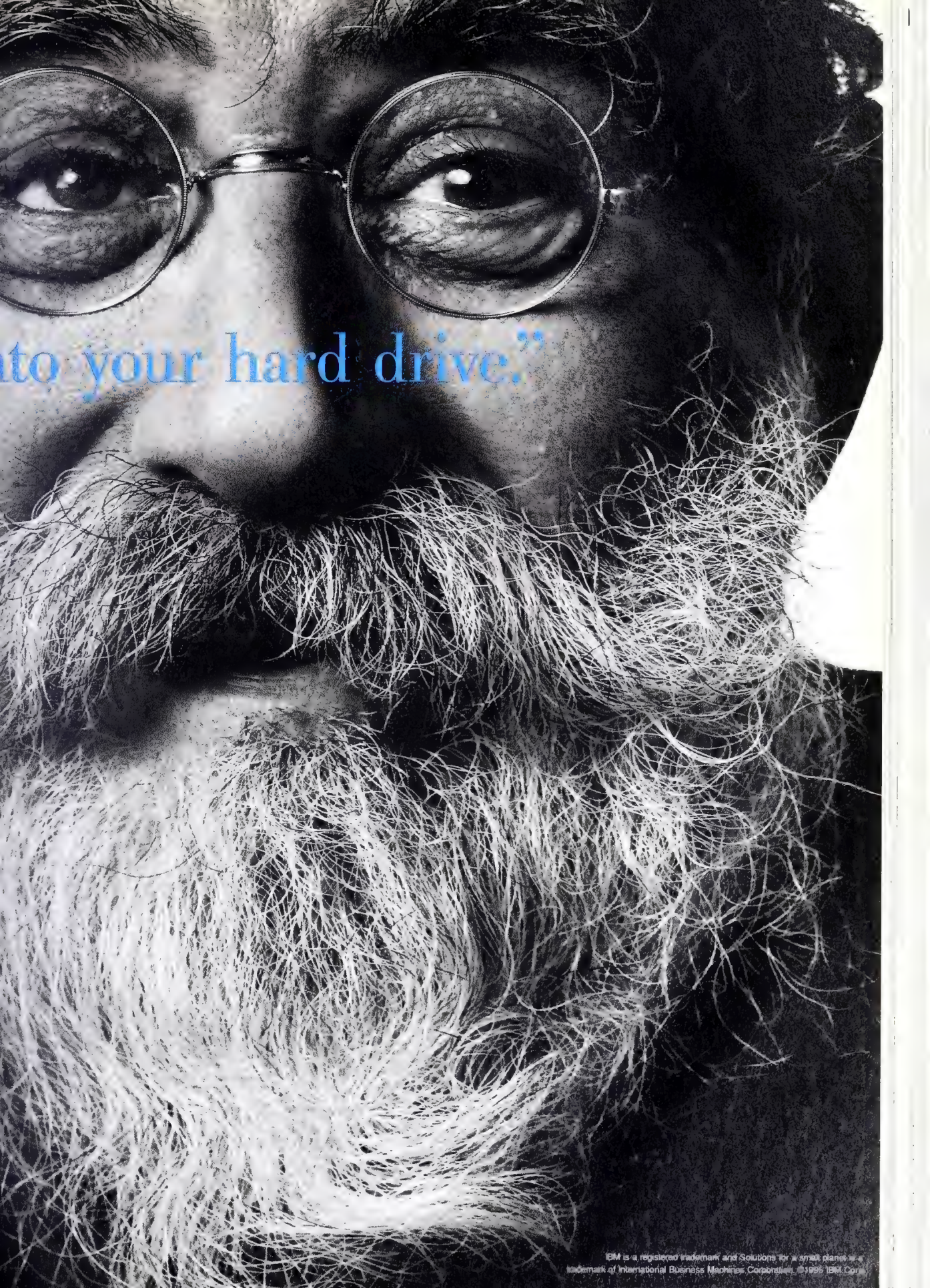
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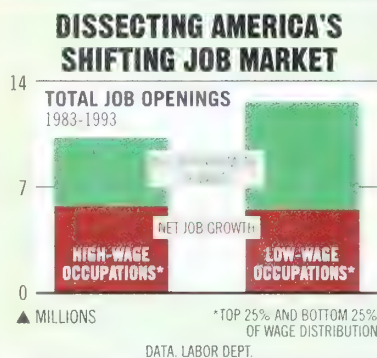
BY GENE KORETZ

## A TREND TOWARD QUALITY JOBS?

Yes, but not as strong as thought

Last year, the Labor Dept. issued a report that suggested that the structure of the U.S. workplace was rapidly shifting toward high-quality jobs requiring a skilled workforce. While most job growth was still in industries with low overall wages, the agency noted that many of the new hires in those industries were for high-paying jobs. Some 40% of jobs added from 1988 to 1993 were in occupations such as managers and professionals, with pay in the top 20% of the wage distribution.

Now, however, a new study by Labor Dept. economist Neal H. Rosenthal covering the 10 years from 1983 to 1993, paints a less optimistic picture. Of the



19.7 million rise in employment during the decade, he reports, high-paying jobs with median wages in the top 25% of the pay range accounted for a disproportionate 29%. But low-wage jobs in the bottom 25% of the pay range grew just about as fast (chart).

Looking at total job openings—stemming from both employment growth and the replacement of workers who have either left the labor force or changed occupations—the picture is even less upbeat. The data indicate that 60% of the 20.9 million net replacement openings filled over the 1983-93 period (and 54% of the 41.6 million total job openings) were in occupations in the bottom half of the pay range. As for educational requirements, Rosenthal estimates that some post-secondary-school education was required for 45% of the new jobs created since 1983, but for only a third of total jobs filled.

The bottom line is that the quality of

U.S. jobs has been improving—but at a glacial rate in terms of the overall wage structure of the economy. The Labor Dept. data indicate that only 1% more of all jobs were in the high-paying top 25% of occupations in 1993 than in 1983.

## SILVER LINING IN A FLAWED CPI

Less inflation implies more growth

Economic observers are so excited by the deficit-cutting possibilities created by a new report on the consumer price index that they may be overlooking the rosier picture it paints of the U.S. economy's past performance.

According to a blue-ribbon panel of economists advising the Senate Finance Committee, the CPI as presently constituted is likely to overstate inflation by about a percentage point a year over the next decade. By correcting this upward bias, the government could save itself a cool \$634 billion over the 10-year period and cut the projected federal deficit in the year 2005 by about \$140 billion—mainly through smaller outlays for Social Security and other inflation-adjusted federal programs.

Just as intriguing, however, is the finding that the CPI has likely been overstating inflation for two decades, with the recent upward bias as high as one and a half percentage points. As Robert J. Gordon of Northwestern University, a member of the advisory group, notes: "This implies that both real wages and real consumption have been posting greater growth than reported."

It also implies that the gross domestic product—at least, the two-thirds of GDP representing consumption—has been growing faster than reported, as has productivity. At the least, this suggests that the Commerce Dept.'s coming downward revisions in productivity growth will be overdone (page 114), and that real interest rates and money supply growth are higher than appreciated.

Such calculations may be reassuring, but no one expects the panel's findings on the CPI to result in a revision of past economic statistics. Rather, the group's final report, due next June, is likely to inspire steps to make the CPI more accurate in the future. If that happens, it's worth noting that beneficiaries of government programs won't be the only ones hurt by a revised CPI. Tax brackets are also adjusted for inflation, so nominal increases in wages will push taxpayers into higher brackets faster than before.

## SMALL FRY ON THE PROWL

More plan to grow via acquisition

Hopefully it's only a pause that refreshes. In its latest annual survey of 400 fast-growing middle-market companies (averaging \$4 million sales), Ernst & Young found that 41% plan to raise more capital next year, down from 63% last year and the lowest percentage in five years.

What's more, just 42% of those seeing added capital intend to use it to introduce new products and services—at least in the seven-year history of the survey. Instead, companies are becoming more acquisition-minded. A solid 44% of those planning to raise capital say they will use it to make an acquisition.

## THE WORLD'S PRICIEST SPACE

Bombay is now higher than Tokyo

Dollar rents for prime urban office space around the world continue to fluctuate, reports Colliers International, a real estate consultant and brokerage. Its July survey of effective office rents (including operating costs, taxes, and landlord concessions) in central business districts reveals that Hong Kong is still the world's costliest city, but Bombay has taken the No. 2 spot from Tokyo's slack market. And recent yen weakness suggests that Tokyo's dollar rents are now down a lot more.

Meanwhile, newcomers to the top

| OFFICE RENTS AROUND THE GLOBE              |       |
|--------------------------------------------|-------|
| EFFECTIVE ANNUAL RENT DOLLARS PER SQ. FT.* |       |
| HONG KONG                                  | \$136 |
| BOMBAY                                     | 124   |
| TOKYO                                      | 102   |
| SHANGHAI                                   | 97    |
| MOSCOW                                     | 89    |
| LONDON                                     | 88    |
| MEXICO CITY                                | 55    |
| PARIS                                      | 52    |
| SÃO PAULO                                  | 30    |
| NEW YORK                                   | 28    |
| MILAN                                      | 23    |
| TORONTO                                    | 16    |

\*JULY '95  
DATA: COLLIER'S INTERNATIONAL

102-city survey coming in at \$8.81 per square foot in Perth, Australia.



JAMES C. COOPER & KATHLEEN MADIGAN

# CAPITAL SPENDING'S FUEL WILL CARRY LESS OCTANE

**U.S. ECONOMY** Four and a half years into this economic expansion, a key pattern is now evident: This business cycle features the strongest performance in corporate investment and the weakest showing for consumer spending in any era in the postwar era.

Although long-term trends in technology, competition, and demographics are at work here, this split between corporate and Household Americas also has important implications for the outlook in the short run. That's because the two sectors, which make up 80% of the economy, will be growing more slowly in the coming year than they did in the past year.

Considering also that the economy will get no help from the tighter mix of fiscal and monetary policy, the outlook heading into 1996 is shaping up to one of frustrating moderation. The National Association of Manufacturers recently went so far as to chide government policy makers for fostering the idea that optimal economic growth is only the

or so now expected. Underlying that forecast: A modest pace of job growth will limit consumer spending. And as profits narrow compared with their strong year-ago numbers, businesses will reexamine their capital budgets.

**BUSINESS SPENDING** will remain the economy's strongest sector, to be sure, but its contribution to growth is going to fall off. The economy will feel that pinch in the coming year. After all, rising demand for equipment and construction contributed 38% of the economy's growth so far in this expansion. Up to now, the upturn in the business cycle and the five structural forces fueling capital spending have been working together. Now, the cyclical factors are turning more negative. A key economic principle holds: Investments are based on the pace of output. With the economy slowing, that means less investment. Indeed, the industrial operating rate has fallen from last year's peak, freeing up more capacity. While financing is cheaper, profits and internally generated cash flow—the preferred means of financing capital projects—are set to slow with the economy. The Commerce Dept.'s latest survey of capital spending plans for 1995 shows that businesses expect to in-

crease their outlays for new plant and equipment by 9.4% (chart). Plans are turning out to be stronger than the 6.6% rise businesses had anticipated when first surveyed back in February, but 1995 intentions are still down from the 12.1% rise posted in 1994.

Even the overall gain, however, masks a split between industries. Manufacturers, which account for 30% of all planned outlays, expect to lift their capital budgets by a whopping 26.1%, up from 7.5% in 1994. In the broader service-producing sector, though, outlays are slowing, and plans outside of manufacturing have been scaled back significantly since the last survey.

Spending in the communications industry, for example, is expected to rise 10.4%, only half the 1994 advance. Expenditures by service companies, supplying personal, business, health, social, and other services, are slated to decline 1% after rising 6% last year.

Inklings of the slowdown in capital spending are already showing up (chart). Despite a strong 4.9% overall advance in new orders for durable goods in August, bookings for nondefense capital goods rose only 2.6%, after declining in three of the four previous months. So far in the third quarter, capital goods orders are far below their second-quarter level, which was below the first quarter. Capital goods orders have not declined for two quarters in a row in more than four years.

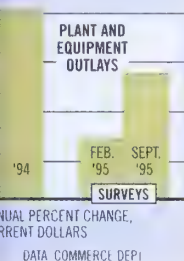
The traditional low-tech areas, such as heavy machinery, will throttle back the most. The recent earnings disappointment at Caterpillar Inc. is a harbinger of the coming slowdown there. But even spending on high-tech equipment, the real leader in the recent investment boom, will see a bit of a slowdown from its rapid pace.

**EARNINGS DISAPPOINTMENTS** at consumer-goods companies seem increasingly likely as well. Consumer spending, while holding up quite well, is nevertheless tracking well below its year-ago pace.

Recent spending gauges suggest a moderate pace for consumer demand. September retail sales at department and discount stores are on track to rise 1.3% from August, according to a weekly survey by the Johnson Redbook Service.

However, households are starting to feel more appre-

## 5 INVESTMENT PLANS MAIN BELOW 1994's



## EQUIPMENT DEMAND FLATTENS OUT





hensive. The Conference Board's index of consumer confidence fell to 97.4 in September, from 102.4 in August. Consumers were less cheery about both the present and the future. Their assessment of current conditions was the lowest level of the year.

The declines could mean that new job worries are creeping into consumers' psyches, especially after the layoffs announced as a part of the big mergers in banking and communications. A more immediate concern: Jobless claims have ticked up in recent weeks.

**OTHER POLLS SUGGEST** that consumers are also leery of policy maneuvering in Washington. But one thing is certain: The economy cannot expect any stimulus from fiscal policy. Budget policy may begin to tighten even before yearend, as Congress and the White House threaten to shut down the federal government on the way toward a deficit-reducing 1996 budget.

With little progress being made on the budget front, many agencies will start to run out of money on Oct. 1. If, as is expected, Congress approves a continuing resolution to keep the government going, that bill may well contain an immediate hit to the economy from spending cuts.

At the same time, monetary policy still looks tight, based on the historical pattern of interest rates. The Federal Reserve decided to leave rates alone at its Sept. 26 policy meeting, but another cut before yearend

seems likely. However, any future cuts may only offset the coming drag from budget reductions.

Moreover, public spending will be more restrictive elsewhere in the world, especially in Europe, one of the U.S.'s key foreign markets. One exception will be Japan, which must try to restart its stalled economy. As a result, world growth will not pick up from its 1995 pace—and it might well be a tick slower.

The U.S. is no longer the poster child of government deficits, according to the Organization for Economic Cooperation & Development (table). In Europe, the need to cut spending results from the Maastricht Treaty, which calls for deficits to run just 3% of GDP by 1997 as a prerequisite for entry into a single-currency Europe. The U.S. sends 46% of its goods to the other Group of Seven countries—56% if you add in all of Western Europe.

In the coming year, areas that have been growth leaders, such as capital spending and exports, will provide less leadership, and those sectors that have been drags recently, including housing and inventories, will provide more support. On balance, it should be a palatable stew, but nothing deserving of a fine wine.

## HOW THE U.S. BUDGET GAP STACKS UP

GOVERNMENT DEFICITS AS A PERCENT OF GDP

|               | 1995 | 1996 |
|---------------|------|------|
| UNITED STATES | 1.8% | 2.0  |
| GERMANY       | 2.3  | 2.2  |
| CANADA        | 3.7  | 2.4  |
| JAPAN         | 4.1  | 4.2  |
| BRITAIN       | 4.2  | 2.6  |
| FRANCE        | 5.0  | 4.1  |
| ITALY         | 7.8  | 6.9  |

DATA: OECD

## JAPAN

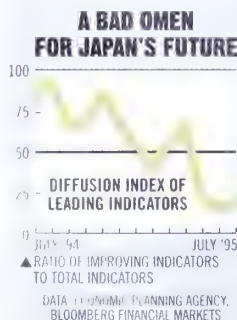
# TOKYO ROLLS OUT ANOTHER RESCUE ATTEMPT

**D**espite a good showing in the second quarter, Japan's economy needs severe help—perhaps more than is contained in the government's latest stimulus effort.

The second-quarter real gross domestic product grew at a quarterly rate of 0.8% after no growth in the first. Private consumption rose, but government outlays fell, and net exports were flat. Some shifts in consumer and public spending reflected a return to normal trends after the Kobe earthquake.

The second-quarter strength is unlikely to last. In August, the trade surplus slipped 1.3% from a year ago, as auto exports unexpectedly plunged 15.6%. Sales at

large retailers were down 0.8% in August. The index of leading indicators stood at 20 in July, the third-straight month that the index was below 50, a signal of weakness (chart).



The government's Sept. 20 fiscal package attempts to pump up the weak economy. The 14.22 trillion yen (\$137 billion) plan includes about 8 trillion yen in "pure water" or new spending, as well as funds for land purchases, small-business loans, and Kobe reconstruction. The cumulative effect of the plan may add about 1.5% to GDP in fiscal 1996.

But the financial markets were disappointed that the plan did not address fundamental problems

such as overregulation, bad bank loans, and tax reform. The Nikkei fell 2.7% in the two days following the plan's release. Even Bank of Japan Governor Yasuo Matsushita said the economy may need more help. And on Sept. 27, the Ministry of Finance released a plan aimed at solving the banking crisis, endorsing for the first time the use of taxpayers' money.

Since the BOJ has cut interest rates close to zero, Japan is using the yen as stimulus. Trade Minister Ryutaro Hashimoto said he wants the U.S. dollar to rise to 110 yen, from 100 yen on Sept. 27. That goal may be too ambitious, but the yen's 26% drop since April will help exports as well as lift corporate profits. Structural reforms, however, will have to take place before Japan's feeble recovery can show more strength.



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## With the right candidate, a third party could have a real shot

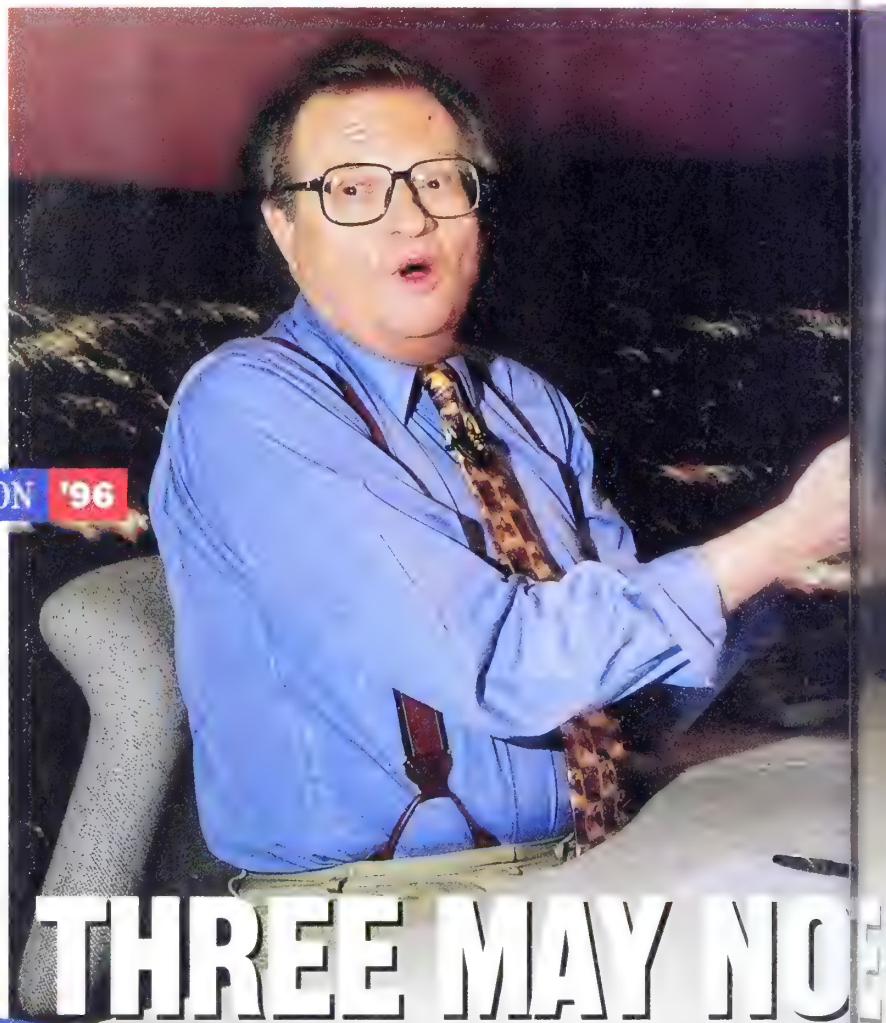
**N**o one said the life of an NPO—Nouveau Political Outsider—was easy. Ask retired General Colin L. Powell and millionaire publisher Malcolm S. Forbes Jr. The pair was just beginning to dance into the carnal tent of American politics when veteran outsider Ross Perot grabbed the spotlight with one of his trademark surprises. On Sept. 25, the Texan announced the formation of the Independence Party, pledging to give centrist voters a choice between dying Democratic liberalism and Republican Big Business as usual.

Appearing on CNN's *Larry King Live* show, Perot outlined ambitious goals for the fledgling organization. By collecting millions of signatures, he hopes to get the party onto every state ballot in time for the '96 elections. Next April, Perotistas will hold a national convention to anoint an independent Presidential slate. By fall, they aim to splinter the two-party system with a platform based on a Cromwellian cleansing of government ethics rules, term limits, campaign finance reforms, and strict budgetary discipline.

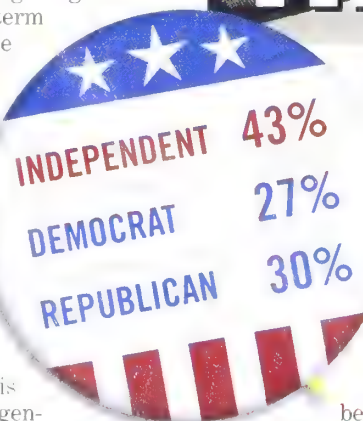
Perot supporters are convinced his money and grassroots organization form a natural basis for a new populist party that's conservative on economic issues but libertarian on social issues. "This country is ready for a new insurgency," says Connie Smith, Washington state director for Perot's United We Stand America (UWSA). But the key to success could be luring Powell onto the ticket: In a new *USA Today*/CNN/Gallup poll, the general beat Clinton running as a Republican (54% to 39%) and ran a dead heat against him as a third-party candidate (table).

Although Republican pols dismiss Perot's gambit as an ego trip, Perot

ELECTION '96



# THREE MAY NOE



### HOW VOTERS LINE UP ...

OF 1,012 ADULTS ON SEPT. 22-24

begs to differ. "I do not need a Third Party," he told *BUSINESS WEEK*. "If I wanted to run for President, I could run as an independent." House Speaker Newt Gingrich doesn't buy that. He calls Perot's third party "a fantasy of delusion."

But Republicans may be miscalculating by assuming that Perot will eventually decide to run again. Aides say Perot now realizes he is too polarizing a figure to serve as more than a cheerleader for the new revolution. "You need a person like Perot, but who can transcend Perot," says Norris Clark, a New Jersey UWSA organizer.

Privately, analysts concede that if Perot stays off the ticket, confines his efforts to fund-raising, and—most im-

portant—attracts a front-rank nominee to head the dissident group, his declaration of Independence could yet shake the Establishment.

How? A new party could lend structure to the heretofore formless populist movement. That in turn could force Democrats and Republicans to put more aggressively for government reforms. And by splitting the '96 opposition to Bill Clinton, the rump party could hurt GOP chances of winning back the White House. "It would just help reelect Clinton," says W. Wayne Allen, CEO of Phillips Petroleum Co., who calls Perot's new pirouette "a disaster."

**SNEAK ATTACK.** All along, the President's political advisers reckoned that his reelection chances were slim unless Perot became a player. "The operative theory," says Democratic consultant Ivid Axelrod, "is that if you're an unpopular incumbent and there are no outlets for disaffection instead of one, that's good."

Still, Clinton aides fret that Perot



## TOGETHER AGAIN: Ross Perot declares his Independence on Larry King Live

Political pros think Perot's supporters will have little trouble gaining ballot access. The greater difficulty will be attracting top talent to the Independence banner. Powell aside, the Perotnistas like Senator Bill Bradley (D-N.J.), former Oklahoma Senator David L. Boren, and ex-Connecticut Governor Lowell Weicker Jr. But these erstwhile champions lack Powell's charisma and name recognition—and most are turned off by Perot's fervent economic nationalism. "The party's anti-NAFTA stance will take away a lot of potential supporters," says former Senator Paul Tsongas. Perot, however, says his new platform omits any reference to trade policy. "That is not on the list," he says.

Beyond doubts about Perot's role are some money concerns. Major-party candidates will enter '96 with public campaign funds and \$60 million war chests. But if he turns UWSA into a party, Perot's ability to underwrite the group will be hampered by election rules that limit gifts to political organizations.

**VOLATILE.** Although obstacles facing the Independence Party are formidable—and Perot's ability to hold his ego in check remains unknown—business lobbyists caution that Corporate America

would be foolish to ignore this latest insurgency. "People who've operated for years inside the Beltway by buying Congress are in for a rough time," predicts John J. Motley, executive vice-president of the Air Transport Assn. "Big Business doesn't understand that this movement could significantly diminish its power."

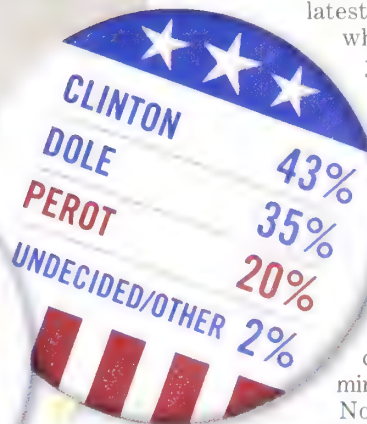
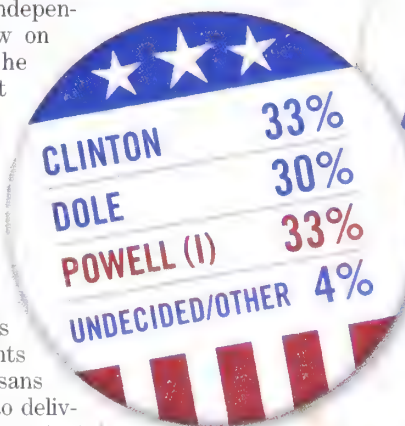
No one can yet divine whether the Perot movement will prove an enduring force, but Republicans and Democrats alike say it's the harbinger of a volatile new era in U.S. politics—one in

which multiparty races may become the norm rather than the exception. That means the two parties that have dominated elections since the Civil War could be at risk—along with the enviable stability of the American system.

*By Lee Walczak, with Richard S. Dunham, Susan B. Garland, Mary Beth Regan, and Mike McNamee in Washington*

# THE CROWD

entice Powell onto the Independence ticket. The anxiety grew on Sept. 26, when Powell said he would seriously consider a Perot bid. "The most important thing is, who's the standard-bearer?" says a Clinton adviser. "If Perot gets Colin Powell, that's one thing. If it's Zasu Pines, that's another." Perplexed Republicans view Perot's third-party bid as a sneak attack that comes just as they are voting on key elements of their revolution. Perot partisans counter that the GOP has failed to deliver the changes that drive their protest movement: a ban on special-interest campaign contributions, stiff new lobbying curbs, a balanced-budget amendment, and term limits. "Republicans can't get it," says New York pollster Donald S. Black. "Perot people see their acceptance of special-interest money as a form of bribery." For months, Perot supporters seethed



### ...WHO THEY'D VOTE FOR TODAY

DATA: CNN/POLLING PLACE POLLS OF 1,000 ADULTS, SEPT. 22-24, LOS ANGELES TIMES POLL OF 937 VOTERS, SEPT. 16-18

over reports that corporate lobbyists were helping to draft GOP legislative initiatives. Anger grew when campaign reports showed Republicans racking up record contributions from business. But the catalyst for Perot's third-party lunge was a series of looming deadlines for winning a spot on the '96 ballot in California and other key states.





## CANDIDATES

# STEVE FORBES: IF DOLLARS WERE VOTES...

But as a late starter, he may face insurmountable obstacles

**M**alcolm S. "Steve" Forbes Jr. couldn't quite contain himself. "I don't want to bore you with an arcane discussion of monetary policy," he apologized to a call-in radio show audience in Des Moines, where he kicked off his Presidential campaign on Sept. 26. "But...."

Then the multimillionaire magazine magnate, the newest of 10 announced candidates for the Republican Presidential nomination, was off and running. The gold standard is "a compass that will keep the dollar stable." The International Monetary Fund is guilty of "economic malpractice." The Treasury Dept. should never have "encouraged the Mexican Central Bank to devalue the peso."

**NO MIRACLES.** Arcane, maybe. But the telephone lines lit up. Callers wanted to know more about Forbes's views on the World Trade Organization and his proposed flat 17% income-tax rate. At a press conference later that day, Rosanne Freeburg, a retired Cedar Rapids kindergarten teacher and grandmother of 10, showed up to question him. She had heard him discuss the gold standard on her car radio and wanted more details.

Only in Iowa. Iowans take their role as the first state to caucus (on Feb. 12) very seriously. And they're neither

haphazard about the process nor uninformed about economics. After all, Iowa farmers traded in derivatives contracts—cattle futures and pork bellies—long before they were hyped (and bungled) by Wall Street.

## ELECTION '96

Straight-talking politicians are favored here. That's why Forbes's slightly rumpled look, his earnest talk of "returning power to the people from whence it came," and his Reaganesque message of "work, faith, hope, family, trust, and teamwork," might turn a few undecided heads.

But running a successful campaign in Iowa requires lots of volunteers to get out caucus voters. And many activists already are committed to other Republican candidates. "We've got to go out and find the traditional voter who has not been active, and juice him up," says William Dal Col, his campaign manager. Even the candidate isn't expecting a miracle. "Given the time I started, I'm not, I'm told, expected to do well here," says Forbes.

That's an understatement. Forbes has no political experience and no field organization. And he doesn't seem to know who to glad-hand yet, either. When announcing his candidacy at the Savery Hotel in Des Moines, Forbes personally greeted every media representative at the press conference—in-

## Malcolm S. Forbes Jr.

**BORN:** July 18, 1947, in Morristown, N.J.

**FAMOUS FATHER:** Malcolm Forbes

**EDUCATION:** B.A. in history, Princeton University, 1970

**OCCUPATION:** President of Forbes Inc.; Forbes Editor-in-Chief

**FAMILY:** Wife, the former Sabina Beekman, five daughters

**"STEVE'S HOBBY IS PUBLIC POLICY," SAYS AN AIDE**

cluding the television cameramen.

The candidate does have some advantages: Forbes says he is willing to drop \$25 million of a personal fortune estimated at \$400 million on his campaign, if that's what it takes. (By spending his own cash, Forbes avoids the burdensome paperwork requirements imposed when a candidate accepts matching funds.) And Forbes plans to make up for his grassroots shortcomings by leaning on talk show and TV advertising.

Is America ready to embrace Princeton plutocrat with a chateau in France, a 151-foot yacht on the Hudson, and an entire island in Fiji? Forbes aides like to point out that he inherited the expensive toys from his father, Malcolm Sr., who died in 1990, leaving control of the entire Forbes media empire to the oldest of his four sons. Steve, as he prefers to be called, drives a station wagon with 100,000 miles on the odometer and doesn't use the hot-air balloons. "Steve's hobby is public policy," insists an adviser.

**"REAL INTELLIGENCE."** In fact, Forbes is gathering some praise from business leaders, if not money and endorsements. Tandy Chief Executive John V. Roach says the publisher "will add some real intelligence to the debate over economic issues." And Stanley Dempsey, CEO of Denver-based Royal Gold Inc., a gold exploration company, is enthusiastic—no surprise—that the candidate has made a return to the gold standard a major campaign theme (page 37). "It's a fresh new idea," he says.

Forbes isn't the first millionaire to try to win the Republican sweepstakes without federal matching grants. In 1980, ex-Texas Governor John B. Connally turned down public financing, spent \$11 million, campaigned hard in six states—and wound up with just one delegate. Given his late start, Forbes will have to struggle to leave Iowa with even that many.

*By Paul Magnusson in Des Moines*

# THE FAKE GLITTER A GOLD STANDARD

a gold benchmark is too rigid for the global economy

, for the good old days of the gold standard: price stability, sound money, and low interest rates. Little later that Republican Presidential candidate Steve Forbes waxed nostalgic return to the past. "As we did throughout our nation's history until the 1960s, we must tie the value of the

to a fixed measure—such as gold, so a dollar today will be worth a dollar tomorrow," he declares. "It's a minute. If life were a gold standard, it would be really so great, but come the U.S. economy dropped it and completely severed links between the dollar and foreign exchange rates in 1971? The loss of the metal's natural luster, including the Federal Reserve Board, say the reading of history doesn't provide the answer. Tying the dollar to gold didn't produce the results in the days that gold's advocates lovingly recall.

But, there were signs of economic recovery after the U.S. ended the gold standard in 1971 (table). There were also economic crises, panics, depressions, and deflation. In fact, the gold standard may have precipitated downturns by keeping money tight and killing demand. And during this century's worst events—the World Wars and the Great Depression—gold standards were dropped. "Maybe the good old days weren't so good," says economist William P. Sterling, a managing director of Sterling Associates, an investment firm.

**OFF-THE-PANTS.** Forbes and his cohorts of gold advocates view history differently. But they aren't calling for a return to a full gold standard, under which a dollar can be converted into a certain amount of the precious metal. Rather, they want to use gold as a benchmark to ensure that the federal

government pursues zero-inflation economic policies.

Here's how it would work: The government would set gold at a fixed price, say the current price of \$385 an ounce. Then the Federal Reserve, using gold as a surrogate consumer price index, would be required to move interest rates to



**1896** In his run for the Presidency, Democrat William Jennings Bryan pledges to end America's adherence to a strict gold standard.



**1971** President Nixon ends the gold standard completely.

maintain the target figure. A rising price would signal inflation, forcing the Fed to raise rates; falling prices would trigger an easier monetary policy.

Why link the world's largest economy to gold? Because it's recognized around the world as a unique commodity that holds its value, argues economic consultant Jude Wanniski, a Forbes adviser. "Gold is a proxy for all

prices," he says. With the Fed conducting monetary policy largely by seat-of-the-pants guesses, "we need a single known rule" for central banks, he adds.

But the simplicity of the rule is not a virtue, it's a major problem, counter critics. Today's complicated global economy doesn't lend itself to an inflexible monetary rule. These days any international crisis could drive up the price of gold without signaling inflation. For instance, when the Mexican peso collapsed last winter, the price of gold jumped. Under a gold standard, the Fed would have been forced to increase interest rates, which could have sent the economy into a recession. "Gold was an ideal standard a century ago but no

more," says former Fed Vice-Chairman Manuel H. Johnson. "You have more speculators, volatile markets, sophisticated traders, fluctuating gold supplies, and too many other variables to depend on one rule."

Critics also say a gold standard assumes that preserving the dollar's value should always be the federal government's top priority. That may be true for people with great wealth, but not necessarily for people in general, who are borrowers rather than lenders. When oil prices skyrocketed in 1973, U.S. policymakers decided that high inflation was preferable to a tight money response that might

have caused a slump even worse than the 1974-75 downturn.

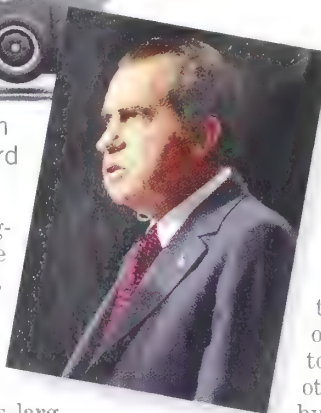
Fed Chairman Alan Greenspan was a gold advocate earlier in his career. But now he, too, sees the limitations of depending on any single standard. He tracks the metal, but as just one of many important indicators for steering policy. Like others who are no longer lured by its sheen, Greenspan has come to a simple conclusion: A gold standard sounds great in theory, but it no longer works in practice.

*By Owen Ullmann, with Dean Foust, in Washington*

## THE GOLD STANDARD'S RISE AND FALL

**1821** Britain adopts the gold standard. The U.S. follows in 1871.

**1933** The Depression forces the U.S. to stop converting currency into gold. In 1946, it relinks the two for trade reasons.



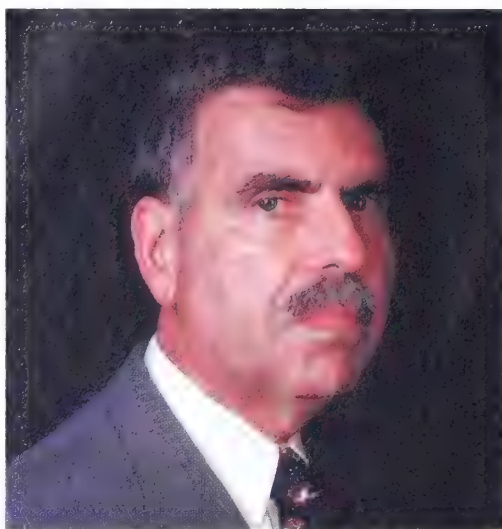


## DEALS

# 'I'M PERFECTLY WILLING TO BE RUN OUT OF TOWN'

Chairman Levin defends the Time Warner-TBS merger

**I**t's not easy being Time Warner Inc. Chairman Gerry Levin. When Michael Eisner bought Capital Cities/ABC Inc. for \$19 billion to create the world's largest media company, Wall Street lavished the Walt Disney Co. chairman with praise. When Levin grabbed back the "world's largest" title with his \$7.5 billion takeover of Turner Broadcasting System, all the business world could talk about was how long it would take for him to lose his job. Recently, Levin sat down with Media Editor Michael O'Neal to defend both the deal and himself.



**Q:** Your joint-venture partner, U S West, and Turner co-investors Comcast and Continental Cablevision have challenged the deal. Any worries?

**A:** Not in the least. There are a lot of people who don't want this deal done. We have a very compelling transaction that has aroused a lot of emotion. We must be doing something right.

**Q:** Others have criticized the deal as dilutive. What's your response?

**A:** Of course the stock went down after we announced a stock transaction. But we've made a confident statement of how we're going to work through the dilution. The conversion of WTBS into a cable station will generate \$100 million a year. And we can distribute a lot of Turner [product] for which they now sell off the rights. If I stopped right there, we'd work it off in a short period of time.

**Q:** Ted Turner and John Malone will both be major shareholders. Do they want your job?

**A:** Ted Turner isn't a Trojan horse. John Malone is a passive investor. He has given us his votes. And [his block becomes nonvoting] if something happens to me.

I'm radically changing the shareholding base of Time Warner to be media-oriented, and I think it's very healthy. You'll have 35% of the company owned by people with one thing in common—they understand the media business and the powerful nature of where it's going. It's a surrogate for when the Luces owned Time or when the Warner brothers owned that company. If you're a [major] shareholder, it's not that you'll automatically agree with me, but you'll understand the context. I'd be out in a

second if I'm not delivering. But there will be an understanding that Time Warner is not some widget company.

**Q:** You've hinted that you want to rid of Time Warner's management fiefdoms. How will you do that?

**A:** This transaction compels a kind of teamwork. In the past, I've never used the word "synergy" because there was more financial mileage in growing individual businesses. The fact that Warner Bros. sold movies to HBO was nice, but that existed anyway, so there was no value creation there. Now, you have a Warner Bros. that is making cartoons for the Cartoon Channel. As instead of selling *Lois and Clark* in

## NEW DIRECTION

"It's going to get worked out... so that there is an organization that is less hierarchical..."

syndication, it should go on TNT or TBS. People will have to be paid and think in terms of: "How do we create value in the networks?"

**Q:** That's fine, but how do you actually change executive behavior?

**A:** Anyone who isn't on the team is out.

**Q:** Why didn't you do that before?

**A:** Had there been an economic reason to do it, I would have. Now the economic reason is so compelling, I'm not going to let anything get in the way.

**Q:** It's been said HBO chief Michael Fuchs is unhappy with his future role. What will he be doing?

**A:** People are picking on that, and it's a mistake. I've made it very clear that I'm not going to make the same mistakes that we made with Time Warner—that is, we negotiated an organizational structure as part of the merger. There was no sensitive appraisal of the needs of the situation. [This time] no one had a fixed assignment. It's going to be worked out in an understanding fashion so that there is an organization that

## LEVIN'S MINEFIELD

**DEBT** Time Warner's \$18 billion debt load—largely left over from the 1989 merger—will be easier to carry thanks to Turner's rich cash flow. But it remains a huge drain that must be reduced.

**SYNERGY?** Infighting has prevented much cooperation between Time and Warner. Turner's assets fit neatly with Time Warner's on paper, but forging real synergy is another matter.

**CULTURES** Time Warner is comprised of fiefdoms where executives are paid a king's ransom to run bureaucracies. Turner is a scrappy, cost-conscious entrepreneurial company. Can they coexist?

**SHAREHOLDERS** Ted Turner gets 10% of Time Warner. TCI's John Malone and Seagram's Edgar Bronfman will both have 9% stakes. If Levin falters, he can count on pressure from this troika.

**PARTNERS** Levin has been struggling to restructure U S West's 25% investment in Time Warner's cable, studio, and HBO assets. Its legal challenge to the Turner deal complicates matters.

hierarchical and more team-oriented—predict to you that everybody will be happy.

*You've been under fire since 1992. How do you deal with that?*

My definition of myself is to do the best thing even if I make a lot of enemies. Time Warner was born into a tradition of angst. At each step [since

then] I've offended somebody—I've even made mistakes. But no one can accuse me of entrenchment or making a power grab for its own sake.

**Q:** People have said this transaction is designed to buy you time. Is it?

**A:** Buying time? I'd walk out this door in a second. I'd love to write the Great American Novel. I think this is a semi-

nal transaction, but I'm perfectly willing to be run out of town if the performance isn't there. I finally want to make a clear break with the past because so far it has been nothing but people getting upset. It will never be the old Warner or the old Time again. It's going to be something totally different, as it must be. I believe I'm on the right track, and I'm very tenacious.

## JOHN MALONE ISN'T POUTING, HE'S PLANNING

For a man used to getting his way, it was a rare admission of futility. "This has been a crummy summer for me," allows John Malone. Not only did the Tele-Communications Inc. chief executive suffer through Denver's hot season but he also watched competing media companies sprint ahead of him in size and reach.

Not that Malone didn't make a handsome deal with Time Warner Inc. By signing on Chairman Gerald M. Levin, Malone parlayed his \$1.4 billion stake in Turner Broadcasting System Inc.

into stock and concessions worth nearly \$3 billion (table). Still, while he and Turner and Levin high-tailed it for the cameras on Sept. 22, Malone found himself cast as a smallish independent in a fast-consolidating land of giants. TCI will only reach one home in seven. By contrast, the Walt Disney Co. and Capital Cities/ABC Inc. merger gives Disney access to nearly every home in America.

**PLAYING CATCH-UP.** But Malone is already plotting to catch up with the big boys. He says he has been talking for months to assorted entertainment companies, including

Seagram Co., parent of Universal Pictures, and Sony Corp. about a range of deals that could include joint ventures to supply programming to subscribers.

Programming is a must for Malone. Mergers between programmers and distributors may make programming, cable's lifeblood, more expen-

sive. That's why Malone secured a 20-year deal to carry CNN and other Turner programs at discounted prices. And that's why he pressured Time Warner to market Home Box Office along with TCI's Encore Media, a package of 15 pay channels. The deal never materialized, al-

U.S. The week before Levin approached Turner, Malone met Murdoch, who jointly owns a pay-per-view system with TCI. "I can't imagine anyone I'd rather be in business with," says Murdoch.

But before Malone can strike a big deal elsewhere, he needs Congress to approve telecom reform that will relax restrictions on the size of cable

companies and their ability to own broadcast properties. With those restrictions lifted, Malone may link up with the likes of Seagram Chairman Edgar Bronfman Jr. to buy a television network, figures

Raghu Ram, an analyst with major TCI shareholder Alliance Capital Management. Further down the road, Ram says, Malone may swap TCI's Liberty Media Corp. unit for Time Warner's cable systems and its 14 million subscribers.

Still, Malone isn't close to any deal yet. And even his sweet deal with Levin could unravel. Fellow Turner shareholders Comcast Corp. and Continental Cablevision Inc. are livid about the riches bagged by Malone and may file suit to block the deal.

But trying to predict Malone's next move is usually

pointless. For now, he must play the role of passive Time Warner investor, forced to turn over control of his shares to Levin by laws that restrict the size of cable companies. But don't expect him to stand pat. Malone is not the type to let a crummy summer mess up his year.

*By Ronald Grover in Los Angeles and David Greising in Atlanta*

### JOHN MALONE'S BIG PAYDAY



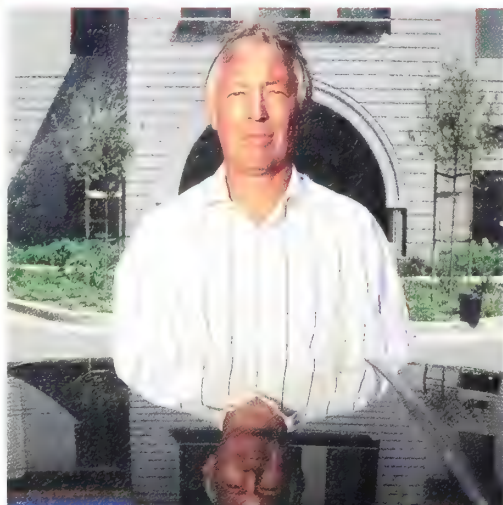
*Here's what TCI's chairman got from Time Warner for his 21% stake in Turner:*

1. Malone's Liberty Media exchanges 65 million Turner shares worth \$1.4 billion for 55.6 million Time Warner shares worth \$2.2 billion
2. Liberty Media gets Turner's 44% stake in SportSouth, a regional sports network, for \$60 million
3. Liberty Media receives an option to acquire Time Warner's Sunshine Network for \$14 million
4. TCI is granted a 20-year deal to carry Turner programming at discount rates
5. TCI receives an additional 5 million shares worth \$360 million for giving Time Warner a six-year option to purchase Southern Satellite, which distributes Turner's WTBS to cable operators

though a joint marketing agreement is possible.

To catch up, Malone needs to bring home a big deal, perhaps linking TCI with Rupert Murdoch's News Corp. The two talked earlier this year about TCI investing in News Corp.'s BSkyB Satellite in Britain, and sources say they have also discussed programming ventures in the





EXECUTIVE SUITE

# KINGMAKER —AND BREAKER

Will Chairman Mike Markkula shake up Apple again?

**A**mong close followers of Apple Computer Inc., he's known as "the kingmaker." And on Oct. 3, when Apple's board meets to look into the company's recent string of product delays and earnings shortfalls, Armas C. "Mike" Markkula Jr., 53, the company's longtime chairman, again will emerge from behind the throne to wield his considerable influence. A few analysts speculate that he will push for a management shakeup as he did when past Apple chiefs were tossed out. Not so, says Markkula. He affirms his backing of CEO Michael H. Spindler, but as usual, he will say little more.

There's little doubt, however, that Markkula is stepping up his involvement in the company. "Mike comes to the surface when things are at a crisis," says John Zeisler, a former Apple executive who is now a senior vice-president at Netcom On-Line Communications Services Inc. Insiders say Markkula is keeping close tabs on management while he pushes for IBM to link its OS/2 personal computer software with Apple's Macintosh operating system and to develop new PCs to run Mac software. (IBM executives say they have no such plans.) In Silicon Valley, meanwhile, speculation persists that Apple may be taken over.

Markkula has steered Apple around tight corners before. Already a millionaire and a veteran of Intel Corp. when Apple was founded in 1977, he wrote

**CLOUT:** His vote ousted Steve Jobs its first business plan and put \$250,000 into the startup. He also drummed up \$3 million in venture financing. When things went sour in 1981 with Apple's first president, Michael Scott, Markkula stepped in to run the show.

These days, Markkula often checks in with Spindler by phone. Soft-spoken and gentlemanly, he never dresses down managers. "He's very open and nonconfrontational," says board member Bernard Goldstein. Adds former Apple research chief Jean-Louis Gassée: "Mike wields influence, not naked power. We're talking about Mr. One-on-One. There are never any witnesses."

Markkula, however, is adept at boardroom intrigue. He cast the decisive vote in 1985 when co-founder Steven P. Jobs was ousted in a power struggle with John Sculley—but only after calling 35 Apple managers to check up on Sculley. In 1993, Markkula was the linchpin in the decision to toss out Sculley after Apple's inventories had soared.

**REDWOODS ESTATE.** In less turbulent times, Markkula's passions range widely. An avid pilot, he owns ACM Aviation, an aircraft leasing company. His major investments include Volant Ski Corp. outside Denver, maker of newfangled stainless steel ski equipment, and Echelon Corp., based in Palo Alto, Calif., which makes home- and industrial-automation chips.

Another consuming interest is his 50-acre spread among the redwoods in ritzy Woodside, Calif. Markkula has taken inventory of the rare flora on the property, which was built by an eccentric 19th century real estate baron. He has also spent more than \$1 million to revamp a Moorish-style 1920s movie theater, complete with a gaggle of the latest audiovisual gear and a tunnel to a garage for guests. Markkula's next job: to convince the town council to change ordinances so he can build an 18,000-square-foot dream house on the land.

Is the new house a sign that Markkula's passion for Apple is waning? Associates insist not, saying he remains bullish. Still, since the start of 1994, he has sold 1.6 million shares, 30% of his holdings. The take among computer-industry gossips: The kingmaker is hedging his bets.

By Peter Burrows, with Kathy Rebello, in San Francisco

## STRATEGIES

# THEN AGAIN, SMOTHER ME

In need of IBM's resources, Lotus gives autonomy the boot

**M**erger plan, take two. Just three months after its \$3.5 billion acquisition of Lotus Development Corp., IBM is mulling a radical revision of strategy.

As part of a three-day management powwow that began Sept. 25, IBM Chairman Louis V. Gerstner Jr. and team met with top Lotus executives to hammer out the thorny issue of how to mesh the vastly different companies. On the table: a proposal by Lotus Chairman Jim Manzi to consolidate the companies' software businesses into one \$12 billion unit.

That's a big about-face. Gerstner engineered the takeover of Lotus last June by promising to keep Manzi on board and Lotus at arm's length from IBM's stifling bureaucracy. But Manzi quickly found that autonomy hampered his ambitions to make Lotus and its Notes groupware program into viable challengers to Microsoft Corp. To do that, Lotus needs IBM's deep pockets, clout with corporations, and technology trove.

"We look at IBM and say, 'Look at the jewels of technology, look at those sources... let us at it,'" says Lotus Senior Vice-President Robert K. Weiler. **DEFLECTIONS?** Manzi hopes to create software behemoth within IBM with himself at its helm. He also is recommending that key Lotus execs be granted broader powers. Weiler, for one, is being considered to head a combined software sales force. Still, insiders say, Manzi is unlikely to win control of IBM's massive mainframe software business.

It's not clear what Gerstner will decide or how quickly. But top Lotus executives—now rich from the deal—may start defecting without quick action. IBM is listening. "Lotus is fundamentally changing the way IBM is thinking," says one IBM executive. The question now: Can it change the way IBM operates?

By Amy Cortese in New York



**MANZI:** Can he carve out a \$1 billion empire?



# RE WE HAVING IN YET?

covery Zone tries to escape a tunnel of losses

had all the ingredients of a bang-up business concept. The company's investors, mentors, and key managers included some of the same people who transformed a bunch of low-cost waste-hauling, video rental, and rotisserie chicken operations into highly successful national businesses. Indeed, in mid-1992 when this company bought Discovery Zone Inc., an indoor playground chain for kids, from its founders, it seemed to bear all of the hallmarks of Waste Management, Blockbuster Entertainment, and Boston Chicken. The strategy was similar, too: Buy out scores of company stores, buy up rivals to become dominant in a hot new business. The similarities end there. Ever since late last year, when Discovery Zone confidently predicted "an outstanding 1995," the company has seemed like a wildered kid lost in a maze of tunnels and colored balls. Awash in red ink, PaineWebber Inc. figures may hit \$100 million on revenues of \$267 million this year, Discovery Zone stock, at \$5, languishes 75% below its 52-week high. On Sept. 18, the company announced it is in default with its banks, led by NationsBank Corp., on about \$100 million in a revolving credit deal. For investors such as H. Wayne Huizenga, Jr., J. Melk, and former Discovery Zone Chief Executive Donald F. Flynn, the episode so far is "enormously embarrassing," says one friend of all three. Now, a new management team is trying to fulfill the company's promise. Huizenga and Melk have left as directors. Berrard no longer has executive duties, although he remains a director. Entertainment giant Viacom Inc. has become Discovery Zone's largest shareholder, with a result of its acquisition of the formerly Huizenga-led Blockbuster Entertainment Group, which itself had been Discovery Zone's largest shareholder by acquiring much of the Flynn stake in mid-1994.



stake in the company. Moore says senior executives are consulting with McDonald's on how to upgrade breakfast and lunch offerings—a major shortcoming. "If you can't find good coffee and muffins, parents may find another place to entertain their child," says Moore.

She has had no shortage of other difficulties to address. Discovery Zone's main failing, say several sources close to the company, was hell-bent expansion with lax controls, capped by simultaneous acquisitions of the 49-branch McDonald's unit and 60 Blockbuster-controlled Discovery Zone franchises. Moore says she found 17 separate pricing systems in use nationwide. Computer and accounting systems were only recently combined. Worse, says former Las Vegas franchisee Stephen W.

## REDISCOVERING FUN.

*Kids were getting bored*

## ZONED OUT



In May, Blockbuster began replacing most senior managers and relocating the company from Chicago to its own base in Fort Lauderdale, Fla. In July, Blockbuster CEO Steven R. Berrard named as president Donna R. Moore, a veteran retailer with experience at Motherhood Maternity Shops, Laura Ashley, and Walt Disney stores. Berrard remains CEO.

**HELL-BENT EXPANSION.** Moore is readying a marketing overhaul that aims to use Discovery Zone's ties to Blockbuster and Viacom to liven up the chain's 340 U.S. branches. Even McDonald's Corp. will get a hand in the remake. McDonald's sold its competing Leaps & Bounds chain in mid-1994 to Discovery Zone for \$100 million in stock—now valued at just \$27.5 million—and a 10%

Littig, Discovery Zone seemed tired. "The kids got bored, and the parents got bored," he says. And on weekdays, business dies: Anywhere from 53% to 68% of traffic is on weekends.

To try to recover, Discovery took a second-quarter write-off of \$72 million to account for severances, flashy but disappointing new light and sound equipment, and lease commitments on closed units. Blockbuster is leading the debt restructuring talks, and executives say they are confident of a deal. Store openings are slowing—to about 10 a year this year and next, about one-third of the aggressive earlier pace.

Moore has big plans. On Oct. 1, she will introduce an annual \$49.95 weekday pass, seeking to build mid-week visits. She also wants to develop activities for single parents while their kids play. Expect cross-promotions with Blockbuster, featuring discounts at Discovery for video rentals, and advertising on Viacom's Nickelodeon cable-TV network pushing Discovery Zone. There are also likely to be tie-ins with the children's division of Viacom's Simon & Schuster book unit. A key aim, says Moore, is simply to avoid disappointing kids and parents. "Our favorite line around here now is, you can't refund a child's birthday," says Moore. If Discovery Zone can live up to that motto, it may yet prove a profitable adventure.

*By Richard A. Melcher in Chicago with Elizabeth Roberts in Miami*



LEGAL FIGHTS

# JUST HOW FREE IS FREE SPEECH DELAYED?

For the third week, a BUSINESS WEEK story is kept on ice

The case traveled abruptly to the U.S. Supreme Court and back. BUSINESS WEEK journalists and lawyers shuttled between New York and Cincinnati, the reporters turned nervous participants in a high-profile constitutional brawl. And on Sept. 27, a corporate attorney for a prominent New York law firm admitted having provided a controversial court-sealed document.

The upshot of it all: For a

third week, BUSINESS WEEK was barred from printing an article based on the sealed document that is part of a suit by Procter & Gamble Co. against Bankers Trust Co. U.S. District Court Judge John Feikens says he will decide by Oct. 3 whether to vacate or make permanent his injunction, first issued on Sept. 13.

The nonaction was unprecedented. U.S. courts historically have quickly overturned lower courts when prior restraint of the press is at issue. Yet on Sept. 21, Supreme Court Justice John Paul Stevens refused on procedural grounds to stay Feikens' order—even though, he noted, "it was not supported by the findings of fact required."

**"TROUBLING."** Stevens' decision drew predictable criticism from news executives, who called it a weakening of the First Amendment. "It's a troubling trend, for all of us," says Jennifer Carroll, executive editor of the Burlington (Vt.) *Free Press*.

Outside America's newsrooms, however, there was far less angst. "Businesspeople see it differently—that the courts put documents under seal for a reason, and they shouldn't be



THE SOURCE: LAWYER STEVEN HOLLEY

disclosed," says Carl A. Ekland, a Denver bankruptcy attorney. "If that diminishes the power of the press, then yes. Other people may see it as just following the rules."

But the hearings in Feikens' court that followed Stevens' ruling dwelled little on First Amendment concerns. Rather, the judge was intent on determining how the breach of court security had occurred—and whether the magazine had acted illegally.

Bankers Trust attorneys argue that the sanctity of the court is at issue and that the publication of the document in question would irreparably damage the bank.

Ironically, though, the breach of security came from within the Bankers Trust camp. In a Sept. 22 conference call with Feikens, attorneys for the bank revealed that messenger records had led them to Steven L. Holley, a young litigation part-

ner at Sullivan & Cromwell, a Wall Street firm acting as Bankers Trust outside counsel. Under questioning at an earlier hearing, BUSINESS WEEK had refused to reveal Holley's identity.

In testimony before Feikens, Holley said he had delivered a copy of the sealed document to Linda Himmelstein, BUSINESS WEEK's legal affairs editor. "I thought that I was complying with a courteous request for a public document," Holley said. "That obviously was a terrible mistake." Holley said he did not realize the papers were confidential until confronted by senior Sullivan & Cromwell partners on Sept. 21 with the messenger records linking him to Himmelstein. He denied Himmelstein's assertion that she called after the papers were delivered on Sept. 21 to tell him of the court seal—even when confronted with telephone records indicating the two had talked.

Holley said he had been reprimanded by the firm, which has apologized to Bankers Trust and to the court. His testimony, meanwhile, appeared to support BUSINESS WEEK's contention that it had done nothing illegal to obtain the document—a view disputed by Bankers Trust attorneys. Ultimately, however, BUSINESS WEEK argues that the legality of the magazine's actions in obtaining the document is irrelevant to the question of prior restraint. "It's clear there's no evidence of irreparable harm... sufficient

to justify a prior restraint," said Kenneth Vittor, general counsel for The McGraw-Hill Companies, BUSINESS WEEK's parent.

Constitutional experts say that BUSINESS WEEK eventually should be able to publish the disputed article. Yet that result may be overshadowed by the fact that Feikens' injunction was allowed to stand as long as it has. Is the First Amendment sacred? Given a more skeptical public and more conservative justices, "I can easily imagine the Supreme Court having a much different attitude toward prior restraint," says Richard Friedman, a law professor at the University of Michigan. The press may turn out not to be free, after all.

By Keith H. Harmonds in Cincinnati

## CINCINNATI STANDOFF The two sides to BUSINESS WEEK's battle



### SANCTITY OF THE COURT

Bankers Trust argues, and the court has agreed, that publication of the document hinders the court's ability to enforce its own orders. The bank also states that its reputation will be harmed irreparably if the information becomes public.

### RIGHT TO PUBLISH

BUSINESS WEEK says a desire to preserve the court's power does not justify prior restraint of publication, which has never been upheld. The press can be censured for disclosing such documents—after publication—but cannot be prevented from publishing.



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## COMMENTARY

By Michael J. Mandel

## HOW IMMIGRATION CAPS CHOKE OFF GROWTH

The latest Washington push to limit immigration is a classic case of how the government can break what doesn't need to be fixed. In the midst of one of the greatest economic booms in recent history—high productivity growth, low inflation, and rising competitiveness—lawmakers are proposing to reduce the number of skilled immigrants to the U.S. by as much as 50%. Who would be hurt most by this move? U.S. high-tech industries, of course—the sector most likely to employ high-skilled immigrants, as well as the sector most responsible for the American economic renaissance.

It's dismaying that this bid to snatch defeat from the jaws of victory has bipartisan support. The latest immigration reform act is about to be introduced before Congress by a Republican, Senator Alan K. Simpson (R-Wyo.), head of the Senate subcommittee on immigration. But the approach was first proposed in June by a commission led by Barbara C. Jordan, the former Democratic representative from Texas.

In addition to cutting the number of skilled immigrants entering the country, the Senate bill and a similar measure in the House of Representatives would reduce the overall number of legal immigrants and narrow the grounds for family-based reunification. But it is the new limits on work-related admissions that reveal the real purpose of the proposed legislation: To cap the number of foreigners coming to the U.S., no matter what benefits they might bring.

**CREATING JOBS.** It's far from clear how Americans would gain from these restrictions. According to a recent Census Bureau report, immigrants with a bachelor's degree or more are entering the country at a rate of about 160,000 per year, an increase from an annual rate of 134,000 in the 1980s. This influx is the equivalent of an enormous gift of human



### The high-tech sector will bear the brunt of limits on skilled immigrants

capital for the U.S. If the average cost of a college education is \$100,000, then the net subsidy from skilled immigrants comes to as much as \$16 billion annually.

Common sense would say that importing workers would take jobs from U.S. workers. But immigrant workers do not just bring their skills, they bring their spending as well, and create new jobs. For example, about one-third of recent population growth stems from immigration. Since about half of all settled immigrants own their homes, it's clear that the home-construction industry—which employs

about 1 million workers at an average wage of \$13 per hour—would suffer without immigrants.

Some argue that cutting the supply of immigrants will force U.S. companies to train domestic workers to fill the positions. But history shows that such "import-substitution" rarely works. In the 1970s, many developing countries closed their borders to imported goods, such as computers and steel, in hopes of protecting their budding domestic producers. But as Brazil and others found, the strategy produced an inefficient and moribund economy.

Moreover, high-tech companies can easily go overseas if they can't get the workers they need at home. For example, Claremont Technology Group Inc., a fast-growing systems integration company, is about to set up a software factory in Ireland employing 60 to 80 programmers. "The U.S. is just not producing enough people to do this work," says Paul J. Cosgrave, Claremont's chief executive. "Stopping the immigration isn't going to solve the problem."

The current wave of immigration-reform proposals does have some redeeming features. For example, the reforms would streamline the lengthy certification process that companies must go through to get a visa for a foreign worker. In exchange, companies would be required to put a significant percentage of the immigrant's salary—perhaps as much as 30%—into helping finance training of U.S. workers.

But in most respects, this is an example of Americans' tendency to back short-sighted economic policies. It may well be in the nation's short-term interest to keep out skilled immigrants who compete for jobs. Over the long haul, though, such restrictions will not help build a stronger economy for the next generation.

*Mandel tracks economic trends.*



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EDITED BY THANE PETERSON

## A SHOCKER AT DUPONT

IT MAY BE A CASE OF GETTIN' out while the gettin' is good: DuPont chief Edgar Woolard, 61, shocked company insiders on Sept. 27 by announcing that he will step down as CEO, effective Dec. 1. The top job will go to longtime No. 2, John Krol, 58, with Woolard remaining chairman of the board. Woolard, who took DuPont's helm in 1992, in recent years has led a restructuring that split DuPont into 20 semiautonomous units and, last year, helped boost earnings some 65%. So far, DuPont is on track for earnings gains of about 25%, to \$3.4 billion, on revenues of \$44 billion this year. Krol, vice-chairman since 1992, is expected

to continue Woolard's basic strategies.

## ALCATEL ALSTHOM IS REWIRING

MORE TELECOM RESTRUCTURING, this time abroad. Serge Tchuruk, the new CEO at France's Alcatel Alsthom, said on Sept. 27 that his company will lose \$256 million for the first six months of 1995 and admitted that the world's largest telephone-switch maker probably won't turn a profit before 1998. Restructuring charges by then are likely to hit \$3.7 billion. Add goodwill write-offs of up to \$2.5 billion and the total bill will top \$6 billion. "We're doing a cleanup operation," says Tchuruk, who took over last May after a series of scandals forced former CEO Pierre Suard to resign.

## CYRIX OUTPACES THE PENTIUM

FINALLY, NO. 2 GETS A BREAK. Cyrix, the Avis among cloners of Intel chips, got a boost on Sept. 25 when market leader Advanced Micro Devices disclosed that its version of Intel's Pentium chip won't be ready until the second quarter of 1996. Taking its cue, Cyrix plans to announce on Oct. 9 that in December it will ship a speedy new Pentium-compatible chip that will give AMD—and Intel—fits. Reason: it is 1.2 to 1.3 times faster than an equivalent Pentium. Analysts say Cyrix, with about 7% of the 486 chip market, could snatch up to 10% of the Pentium market next year.

## FREDDIE NO-FRILLS FLIES AGAIN

REMEMBER FREDDIE LAKER? He's the Brit whose Skytrain service between New York and London launched no-frills

## HEADLINER: VAMP

## CHANEL HITS THE NAIL ON THE HEAD

Madonna and Uma caught on over a year ago. Fashion victims on the coasts were hip to it last summer. By now, any woman who has a passing acquaintance with *Vogue* knows it is the fall's must-have.

The object of their desire: Vamp, a nail color by Chanel. Once a choice only Elvira would make, the \$15 black-red polish is so hot it is sold out at many of Chanel's 500 U.S. cosmetic counters. "It is a can't-live-without-it phenomenon," confirms a Chanel spokeswoman.

Vamp first appeared on the Paris runways in

March, 1994, after a Chanel makeup artist mixed up a batch backstage. Vamp's

success is a product of the industry's back-to-glamor strategy, says Prudential analyst Bonita Austin. After seven years of flat sales, 1995 cosmetics unit volume

is up 2% and prices 5%, she says. Chanel doesn't reveal sales, but it says Vamp has doubled its nail-color business.

For the Vamp-aware, getting the polish is what matters. The next challenge: landing a \$19.50 tube of Chanel's brand-new lipstick, Very Vamp.

By Deidre A. Depke

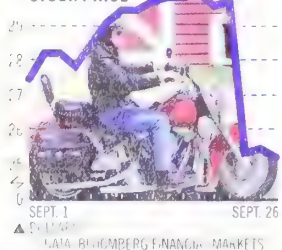


## CLOSING BELL

## VROOM! GLOOM

Given that Milwaukee-based Harley-Davidson has a 6- to 24-month order backlog for cycles, shareholders should be in hog heaven. But shares fell 15%, to just over \$25, after a Sept. 21 announcement that third-quarter sales of parts and accessories will disappoint. The problem: Harley's apparel isn't selling well. Investors may be overreacting, analysts say: Apparel makes up only 35% of Harley's parts and accessories biz, which has been expanding at a 25% annual compound rate for nine years.

### HARLEY-DAVIDSON'S STOCK PRICE



air travel in 1977. Now, he's back. He's planning a December launch of a three-jet fleet that will fly between England and Florida—just in time for winter vacationers. Skytrain collapsed in 1982 amid fierce price-cutting, but Sir Freddie has a deep-pockets backer for the latest reincarnation of Laker Airways: Texas oil millionaire and Coastal Chairman Oscar S. Wyatt Jr. The pair have been friends for 30 years. If the sunshine route takes off, Laker hopes by May to expand the airline's service to Italy and Germany.

## A NEW C-NOTE TO FOIL CROOKS

ATTENTION, HIGH ROLLERS: On Sept. 27, the Treasury and the Federal Reserve unveiled a redesigned \$100 bill, due to enter circulation early next year. The most visible change: a larger, off-center portrait of Ben Franklin. To

stymie counterfeiters, the \$765,000 redesign adds security features such as ink that shifts color from green to black when viewed at an angle, a security thread that glows red in ultraviolet light, more microprinting, and new watermark. Similar overhauls are in the works for the \$50, \$20, \$10, and \$5 bills. Treasury Secretary Robert Rubin and Fed Chairman Alan Greenspan stressed the old \$100 bills won't be recalled or devalued.

## ET CETERA...

■ Baltimore Gas & Electric and Potomac Electric Power are merging.

■ More consumer-product restructuring: Dial plans to close six plants, lay off 700.

■ Argentina's President said Economy Minister Domingo Cavallo will stay on.

■ Microsoft signed with Paramount to offer *Star Trek* over its new online service.

# Countless business-to-business media decisions were made last year. This is for those who made the best.

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EDITED BY OWEN ULLMANN

## THE QUIRKY SUPPLY SIDER WHO'S SHAPING TAX POLICY

**W**illiam V. Roth Jr., the Senate Finance Committee's new chairman, hardly cuts an imposing figure. An introvert known for his quirks—he campaigned last year in the constant company of his two Saint Bernards, Hagar the Horrible and Thor-Tsunami—the 74-year-old Delaware Republican has rarely captured the limelight during his 25 years in the Senate. No wonder Capitol Hill wags are dismissing him as a caretaker chairman—who will be the lapdog of Senate Majority Leader Bob Dole (R-Kan.).

That is a snap judgment critics may regret. "If anybody thinks he's Milquetoast, they'll soon learn better," says Grover G. Norquist, president of Americans for Tax Reform and a backer of the GOP revolution of House Speaker Newt Gingrich (R-Ga.). "He's a strong guy with strong beliefs."

Those convictions will soon go on display as Roth reshapes the tax bill that will emerge from Congress this fall. His predecessor as chairman, Bob Packwood (R-Ore.), was a moderate who preferred deficit reduction to tax cuts and dealmaking to ideology. Roth, by contrast, is an ardent supply sider who co-authored the 1981 Kemp-Roth tax cuts, which became the centerpiece of Reaganomics. "I've always been a strong supporter of tax cuts and will continue to be," he vows. Such talk has cheered advocates of significant tax reductions. "We have a chairman of the committee who is really committed to tax cuts," smiles Senate Majority Whip Trent Lott (R-Miss.).

**DELIVERING THE GOODS.** Indeed, in his first weeks running the Finance panel, Roth has pushed three pet projects that were low on Packwood's wish list: a cut in the capital-gains tax rate, inheritance-tax relief, and expanded eligibility for Individual Retirement Accounts. Other Roth priorities: reduction of the alternative minimum tax for corporations and expansion of the home-office tax deduction.

Delivering such bold changes may be tough. Although Congress' budget blueprint calls for a \$245 billion cut over seven years, the final measure Roth will begin crafting in early October may be smaller, because the GOP is having trouble finding all the savings it promised in order to balance the budget by 2002. Does the low-key Roth have the acumen, energy, and respect to cut Packwood-style deals behind the scenes? "The jury is still out on Roth," worries one business lobbyist.

Just another foolish case of underestimating Bill Roth counter his defenders, who point to his bipartisan consensus building on reinventing government legislation last year and regulatory reform this spring. "Somehow, people have the impression that he can't put together a deal," says Senator Alfonse M. D'Amato (R-N.Y.). "I think he's going to do extraordinarily better than people think."

While Dole will guide the committee's consideration of such politically volatile issues—welfare and Medicare—never Roth's specialties—he's given the new chairman wide latitude on taxes as long as GOP targets are met. And Roth's clout seems certain to grow next year as Republicans push for a massive overhaul of the federal tax code. While he hesitates to endorse either a flat tax, as proposed by House Majority Leader Richard K. Armey (R-Tex.), or a national sales levy, advocated by House Ways & Means Committee Chairman Bill Archer (R-Tex.), Roth insists he'll settle for nothing less than radical change. "Nothing infuriates people back home more than this complex tax situation, which no one understands or feels is a good deal," he says.

Roth's zeal elates GOP revolutionaries, who saw Packwood as an obstacle to slashing government down to size. Now with another committed—though quirky—ideologue on the front lines, victory seems that much closer at hand.

*By Richard S. Dunham, with Mary Beth Regan*



**ROTH:** Veteran tax cutter

## CAPITAL WRAPUP

### RUBIN'S STREET-WISE HIRE

► Treasury Secretary Robert E. Rubin has tapped Assistant Defense Secretary Joshua Gotbaum to develop economic policy for Treasury. At the Pentagon, the ex-partner at Lazard Frères & Co. analyzed the impact of the defense industry's restructuring. Gotbaum is not an economist, but former Goldman Sachs & Co. chief Rubin is partial to his Wall Street experience. Gotbaum would succeed Alicia H. Munnell, now a White House economic adviser.

### JAPANOPHOBIA

► Why is America fixated on Pat Buchanan's message resonating so strongly with the public? One clue comes from EPIC-MRA, a polling firm in Lansing, Mich. It asked 1,000 voters in late September what percentage of cars and trucks on U.S. highways are Japanese-made. The surprising response: 43% believe that more than half are Japanese. The correct answer: 25%. "Buchanan has struck a chord with what people believe to be true," says pollster Ed Sarpolus.

### OUT OF THE HUNDT

► Federal Communications Commission Chairman Reed E. Hundt was banking on a 20% boost in his '96 budget for new chores arising from the telecom-reform bill Congress likely will pass this fall. Fat chance. The Senate rebuffed his request for \$224 million, offering to keep FCC funding at the current \$185 million. The House wants to trim it to \$148 million. Hill budgeteers will likely split the difference. Now Hundt is bracing for dozens of agency layoffs.

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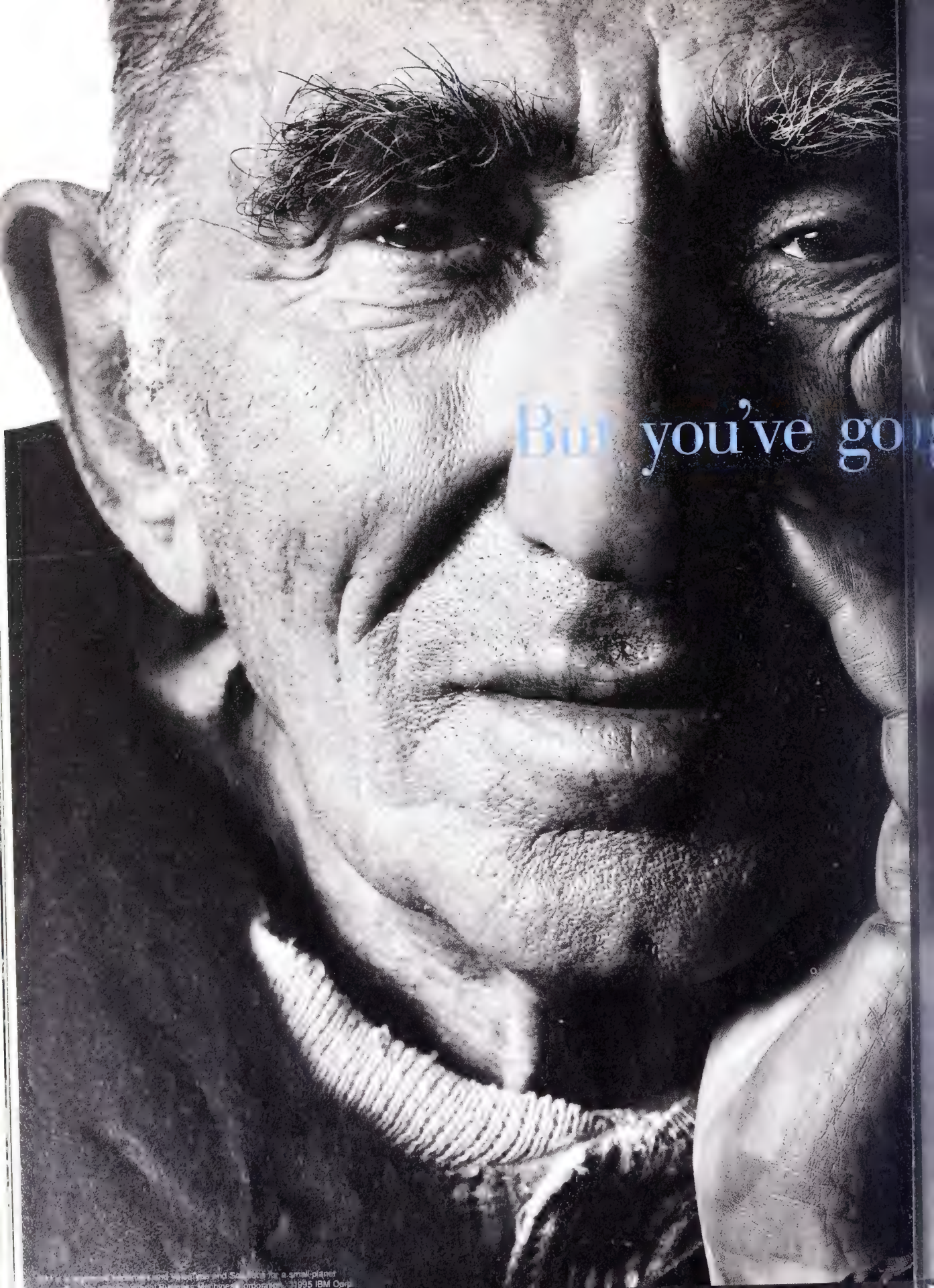
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## GERMANY

# THE TOUGHEST JOB IN EUROPE

Can Ron Sommer transform bloated Deutsche Telekom in time?

**R**on Sommer is a man in a hurry. Even before his first official day as CEO of Deutsche Telekom, Sommer was locked in negotiations in Paris for a deal crucial to the success of Europe's largest telecommunications company. Skipping dinner at Maxim's, he worked far into the night with France Télécom CEO Marcel Roulet and Sprint Corp. CEO William T. Esrey, hammering out details of the Europeans' plan to take a 20% stake in Sprint and launch a global service for corporate customers. The next day, May 16, he reported for work at Telekom's Bonn headquarters late and haggard. But he had pushed the venture one step closer to completion.

Sommer's sense of urgency is justified. There aren't enough hours in the day for his job, possibly the toughest in Europe. He has to ignite a competitive spirit in workers long coddled by Germany's biggest monopoly, lay the groundwork for massive cost-cutting, prod the company to serve customers it long took for granted, and woo investors—all in an unbelievably tight time frame. On Jan. 1, 1998, the European Union is set to throw open the Continent to unfettered competition in telecommunications.

**FIZZLE.** But the key event will come next summer, when Telekom will start privatizing in a \$10 billion stock offering, Europe's biggest ever. Sommer has only a handful of months to convince investors that the company will be ready to compete against the likes of AT&T, British Telecommunications, and new domestic rivals. If any of Sommer's efforts falls short, the stock offering could fizzle, humiliating the government, which will remain a large shareholder, and dealing the company a major blow.

No wonder Sommer gets only five hours of sleep a night these days. A 46-year-old *Wunderkind* who achieved dramatic results at Sony's European and U.S. operations, Sommer has technical brilliance and marketing savvy. But he has never had a job like this. Sommer may have to cut up to 60,000 jobs, a quarter of Telekom's workforce—a painful

task that would cost plenty and require political muscle from Bonn.

And that's just the beginning. After privatization, he'll have to raise profits enough to cover \$86 billion in debt and pay a dividend. He may have to slash prices in half to meet competition. On top of all that, he has to begin offering the state-of-the-art services in multimedia that global corporations demand. Once deregulation takes place, Sommer will face rivals that have a 10-year headstart operating in deregulated markets.

Given the hurdles this \$45 billion company must overcome in just two years, it's not clear

any manager could pull off the transformation in time. When Telekom chief Heilmut Rieke resigned in December, an urgent search for his successor was launched. The job was deemed so daunting no insider stood a chance. Sommer then president of Sony Europe, won with his international credentials: He is a fluent speaker of French and English who had worked for Europeans and Japanese in the U.S. and on the Continent.

Sommer now has to prove his global experience can bring Telekom up to world class. "The company has an extremely high level of knowhow," he says, "but it needs to be



## SOMMER'S CHALLENGE

By 1998, he must ignite a competitive spirit among workers and managers long used to monopoly



customer friendly." Even after deregulation, Telekom will be the dominant player in Europe's largest market. Its work is finally being digitalized. With Europe's biggest cable system, Telekom is positioned to offer multimedia services. Its weaknesses are also striking. On mundane matters such as installing lines fast, Telekom has yet to meet U.S. standards. Processing orders for equipment, service upgrades, and installations are, says one Telekom technician, an "absolute disaster."

**OPERATE NEED.** Sommer's strategy is an attack on all fronts. First, he is working to secure regulatory approval for joint ventures with France Télécom and British Telecom, key to meeting his goal of generating 20% of sales from international sources by 1999.

Sommer needs these joint ventures so badly that he has reversed Telekom's opposition to any liberalization of the German market before 1998. If Germany lets foreign competitors into the market before then, European and U.S. regulators are expected to sign off on the deals.

Inside Telekom, Sommer is sending clear signals that the company must gear up to compete on price and service.

Weeks into the job, he announced a 30% price cut for calls to North America. Telekom also cut prices on leased lines to mobile phone operators by up to 50%. Under Sommer's prodding, branch managers are trying to speed up service. It takes 12 days to hook up new phones. The goal is to provide next-day hookup.

In a move that reflects his experience marketing Sony Walkmans, Sommer has told managers that he wants Telekom to generate the brand awareness of a Coca-Cola or IBM. "I want us to be recognized as a great company," he says. But changing the company's image will never work unless Sommer can motivate his employees to flourish in a deregulated environment. That's like moving a mountain. Says Stefan Doeblin, managing director of MFS Communications, a corporate network provider in Frankfurt: "Sommer is pro-competition. But when you talk to lower levels of management, you still run into problems."

Still, Sommer's no-nonsense approach is setting the tone for his senior executives, who must meet new performance criteria or be prepared to step aside. Sommer isn't one to mingle. Four months into the job, he hasn't eaten in the can-

teen, preferring a quick salad in his office. "I'm no cheerleader," he says. "But my optimism can give [employees] their optimism back."

Optimism has always been Sommer's strong suit. Born in Israel, to a German father and Russian-Austrian mother, Sommer moved with his family to Vienna when he was 7. At 18, he fell in love with America on a trip to New York. Returning to study math at the University of Vienna, he realized research wasn't for him. He sped on to complete his doctorate at age 21.

Unable to afford the tuition for a coveted Harvard MBA, he moved to New York in 1972 and joined Q 1, a tiny company trying to invent a personal computer. Sommer scoured Europe for investors and zeroed in on German entrepreneur Heinz Nixdorf, clinching the deal after dogging him for months. Although the computer didn't pan out, Nixdorf was so impressed with Sommer that he hired him to rustle up new business for his computer company. By age 27, Sommer was running Nixdorf's Paris operations. Recruited in 1980 to Sony, he went on to become president of the German unit in 1986, taking it from sixth to first in market share. In 1990 he became president of Sony Corp. of America, where he accelerated growth. Then he returned home to head Sony Europe, where he boosted sales 10% per year.

**TIME AND AGAIN.** For all his energy, though, Sommer seems to be moving slowly on the labor issue besetting Telekom. Although he has met with union officials, the first big meeting with the works council to discuss restructuring takes place only in December. Sommer wants to boost productivity by more than 50%, partly through a plan to buy out up to 60,000 workers through early retirements and severance packages. But the union so far has only agreed to cut 30,000 jobs, a sign of potential trouble.

The labor issue may haunt Sommer when he begins pitching Telekom's stock offering to investors in Europe, the U.S., and Japan. Fund managers fear pressure will keep employment levels unrealistically high. "If the labor problem is not resolved," says Michael J. Mahoney, portfolio manager at G.T. Global Telecom Fund, "for me to buy, they would practically have to give me the stock." Telekom wants to sell an additional \$10 billion in stock in 1998.

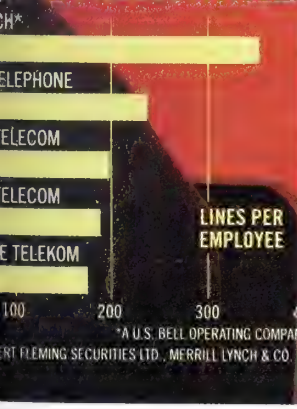
In this supercharged atmosphere, every step Sommer makes is critical. Still, time and again, Sommer has achieved stellar results with a simple philosophy: "It's not magic. You just have to do it." He's about to meet his ultimate test.

*By Karen Lowry Miller in Bonn, with Gail Edmondson in Paris, Larry Armstrong in Los Angeles, and Christopher Power in New York*



TELEKOM'S NETWORK IS EXCELLENT, BUT CUSTOMER SERVICE HAS A WAY TO GO

## DEUTSCHE TELEKOM LIVES IN PRODUCTIVITY...



## ... AND SOMMER HAS A DAUNTING AGENDA

**COST CONTROL** Payroll of 225,000 employees must drop by 27%.

**COMPETITION** Telekom loses all its monopolies in 1998.

**POLITICS** Sommer must lobby the government to set up favorable regulatory environment.

**STOCK OFFERING** Telekom must woo investors to buy \$10 billion in shares.

DATA: BUSINESS WEEK





HONG KONG

## IS GORDON WU STRETCHED TOO THIN?

The maverick developer is juggling projects worth \$30 billion

For commuters used to battling Bangkok's traffic jams, the scenes depicted in a newly released promotional video seem like a dream. Relaxed Thai yuppies arrive cheerfully at their offices, return home early to their children, and cuddle in front of a TV—all because of the \$3.8 billion Bangkok Elevated Rail Transit System (BERTS) being built by Hong Kong-based Hopewell Holdings Ltd. Gushes the voice-over at the end of the video: "BERTS means happiness."

To Hopewell managing director Gordon Y.S. Wu, however, the Bangkok project so far has meant nothing but headaches. Since he signed the deal in 1990, Wu, 59, has had to shuttle back and forth to Bangkok to fend off attacks by Thai technocrats, opposition politicians, and the state-owned railroad. The project, only 10% complete, is three years behind schedule.

Bangkok is just one of many trouble spots for the maverick developer, who has spent much of this year trying to untangle problems with projects and proposed deals totaling more than \$30

billion from the Philippines to India (table, page 57). On Sept. 20, Hopewell fueled investor fears that Wu's empire is suffering a capital crunch with an announcement of a surprise 14% drop in profits and a cut in dividend payments. Hopewell also disclosed that it had injected an additional \$770 million into its partially completed superhighway in China's Guangdong province, bringing total investment to \$1.5 billion. The additional funding is to finance major design changes.

**COOL CUSTOMER.** The news stunned investors. Hopewell's stock fell 8% in one day. The revelation that Hopewell has pumped so much capital into the Guangdong highway left many analysts wondering how much it has poured into other projects. "The market is waiting to see what Gordon pulls out of his hat next," says analyst David Barden at Baring Securities (Hong Kong) Ltd.

While others may be worried, Wu claims to be unconcerned. "All my life I've been second-guessed," he says coolly, wearing his usual short-sleeved shirt

**OVERBUDGET OVERPASS:** A Chinese highway has cost \$1.5 billion—so far

open at the collar. The Princeton-educated engineer, who for years has defied skeptics by pioneering privately financed hotels and power plants in China, dismisses predictions that Hopewell will be forced to pull out of Bangkok and sell hundreds of millions in assets. He maintains that he is working behind the scenes with government leaders to solve problems with his other infrastructure projects.

But given the lack of transparency in policymaking in Asia, not all analysts are convinced by Wu's assurances. Some fear he has committed to too many undertakings in too many places in too short a time. Not only has the expansion put a strain on his financial and human resources, they say, but Wu's penchant for publicly criticizing government foot-dragging is jeopardizing one of his chief assets: his strong personal connections in Asia. If the political tide turns against Wu, warns Michael Green, executive director at Nomura Research Institute Hong Kong Ltd., Hopewell may have to unload assets such as his 55% stake in Consolidated Electric Power Asia (CEPA), spun off by Hopewell last year.

Wu's critics point to the Guangdong superhighway as an example of his mistakes. Hopewell "didn't do its homework before going in with both guns blazing," says Green. Under the original design, Green charges, one 20-mile stretch was to be traversed by a series

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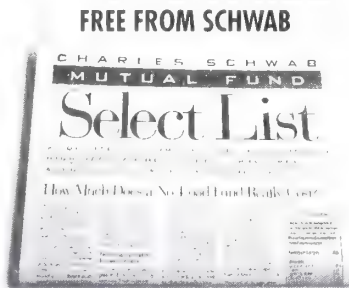
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bridges connected by flat highway. But after work began, engineers said the ground was too soft. To avoid ever-ending repairs, the highway was elevated along the entire section—adding some \$230 million to the cost. Then, when it became clear that in the short term, passenger-car traffic could not support the road through tolls, Hopewell decided that \$540 million more would be needed to expand nine interchanges to accommodate big bus stations.

**DOUBTERS.** Wu says he anticipated the problems, but that it took time to convince Chinese officials that the more expensive designs were worth the money. The Chinese are also responsible, he says, for the nearly one-year delay in opening the highway, since they were too slow in granting land and approvals. But now officials are cooperating, says Wu.

The two sides signed a memorandum of understanding (MOU) in mid-September to refinance the project. Approval from Beijing won't be a problem, Wu insists. Still, some observers wonder if the MOU means Wu really has a done deal. Baring's London notes that two years ago, Wu had MOUs to build power plants in China. One of the projects has gone forward.

Even more doubts are cast on the BERTS project in Bangkok. Signed with the scandal-plagued government of former Prime Minister Chatichai Choonhavan, the plan involves building and operating a six-lane expressway atop elevated railway and commuter train tracks. Other levels will include re-

tail space that will be developed by Hopewell. But soon after the Chatichai regime was deposed in a 1991 coup, the Hopewell project and a number of transit proposals—many of which overlapped—became ensnared in political squabbles. Wu also has been in constant touch with the State Railway of Thailand over numerous details, such as land rights, the project's dimensions, and Hopewell's share of the profits.

Although Hopewell has already invested more than \$300 million in the venture, the company is far short of its goal of finishing the first 12-mile section by yearend. But the new government has placed BERTS on a fast track so that needed sections will be finished by the Asian Games in 1998. And Thailand's King has called on Bangkok to



## Wu's Troubled Deals

| PROJECT                              | COST<br>BILLIONS | STATUS                                                                                                |
|--------------------------------------|------------------|-------------------------------------------------------------------------------------------------------|
| <b>BANGKOK<br/>MASS-TRANSIT LINE</b> | \$3.8            | Plagued by disputes with Thai government; financial viability in doubt                                |
| <b>CHINESE<br/>POWER PLANT</b>       | 1.9              | Startup of 1,980-megawatt Shajiao units delayed by equipment failures                                 |
| <b>GUANGDONG<br/>SUPERHIGHWAY</b>    | 1.5              | 75-mile tollway needs refinancing to cover \$770 million in new costs                                 |
| <b>INDIA POWER<br/>FACILITY</b>      | 12               | 10,560-megawatt Orissa complex stalled by backlash against foreigners                                 |
| <b>PAKISTAN POWER<br/>VENTURE</b>    | 5.2              | First phase of 5,280-megawatt complex approved but needs financing                                    |
| <b>PHILIPPINES<br/>POWER PLANT</b>   | 1.5              | Winning bid for 1,200-megawatt plant revoked by Manila in dispute over use of Westinghouse technology |

DATA: BUSINESS WEEK

solve its traffic crisis as soon as possible. That means clear sailing, Wu contends: "They have an urgent need, and the King has spoken."

Not everyone sees it that way. Thailand has a long tradition of scuttling major infrastructure contracts with each change in government, and the ruling coalition headed by the Chart Thai party is seen as precarious. "Hopewell seems to be making little progress resolving key issues," says a U.S. investment banker involved in a rival mass-transit project in Bangkok. "The project is far too expensive to be feasible."

Wu's worries haven't been nearly as severe with his Asian power projects. But he hasn't completely escaped the political problems that have plagued private providers such as Enron Corp. and

General Electric Co. In July, Philippine state-owned National Power Corp. revoked CEPA's contract for a 1,200-megawatt gas-fired plant because the turbine to be supplied by Mitsubishi Heavy Industries Ltd. uses technology from Westinghouse Electric Corp. Manila has blacklisted the U.S. company over allegations that it bribed late dictator Ferdinand Marcos in the mid-1980s to land a nuclear project, a charge Westinghouse denies. CEPA may contest the move in court, but it hopes the dispute will be solved through negotiations between Westinghouse and Manila.

**A BEST BET.** In the investor community, Wu still has his share of boosters. Many of his financiers are convinced that his Chinese toll road is a winner in the long term and that the government has too much at stake to let the project fail.

Earlier this year, Hongkong & Shanghai Banking Corp. committed a sizable loan, and Japan's Kanematsu Corp. bought 2.5% of Hopewell's 40% stake for \$125 million.

Wu's CEPA is regarded by many analysts as the best bet in Asia's frustrating, but hugely promising, power sector. With construction about to begin on a fourth plant in the Philippines and another in China, CEPA's operating profits are expected to climb from \$77 million in the fiscal year ended June 30, 1995, to \$227 million in 1996. CEPA has secured government approvals and financing for a \$1.8 billion coal-fired plant in Indonesia to be completed by 1998. It also seems to have wrapped up its deal to build the first of five planned

units in Pakistan. Says Jardine Fleming Securities Ltd. analyst Sheldon F. Kasowitz, who predicts CEPA's net profits will approach \$500 million by 2000: "Gordon Wu remains the only one with a track record in private power in Asia."

Wu is confident that his record of deals and the network of contacts he has built in Asia will enable him to solve his difficulties in the region. Still, with policymaking in Asia notoriously opaque, investors have little more than Wu's word that he has the trust of the region's governments. As doubts increase and the financial stakes grow higher in his Asian megaprojects, the question is whether they will keep their faith in Wu's bargaining skills.

*By Pete Engardio in Hong Kong, with Robert Horn in Bangkok*





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JAPAN

## ANOTHER BILLION DOLLARS FALLS THROUGH THE CRACKS

A scandal at Daiwa with a disturbing resemblance to Barings

Last July, Toshihide Iguchi let go of a \$1.1 billion secret. Daiwa Bank Ltd.'s Treasury-bond trading chief in New York, a boyish-looking 44-year-old nicknamed "Tosh," mailed a written confession detailing an 11-year chronicle of financial deceit to Daiwa President Akira Fujita in Osaka. Iguchi marked the letter "personal and confidential." But its contents hit the bank's headquarters with the force of a tsunami.

The rest of the world found out why on Sept. 26, when federal prosecutors charged an impassive Iguchi, clad in

With \$180 billion in assets to offset the T-bond losses, Daiwa won't share the fate of Barings, which was absorbed by the Dutch financial-services group ING. Still, the loss was ever the more unsettling given earlier trading messes at Kidder Peabody, Salomon Brothers, and Chemical Bank—and financial scandals involving Japanese banks and corporations going back to the 1980s.

In an age of mushrooming global trading, the stakes are getting bigger, however. Events occurring in one time zone can easily have huge repercussions

taking the wind out of Japan's new plan to aid troubled lenders. Unveiled Sept. 27, it includes toughened disclosure rules, refloating Japan's Deposit Insurance Corp. with public money, and perhaps a Resolution Trust Corp.-style vehicle to clear out problem loans.

The aim of the plan is to restore international confidence in Japanese banks. But now many analysts are wondering whether some are up to the job of managing their day-to-day affairs. "If they can't control trading even in simple instruments, how about the more complex ones?" wonders Henry T.C. Hu, University of Texas law professor and trading expert. "You have to engage a presumption of incompetence."

**ENTER THE FBI.** Just how much Daiwa knew about Iguchi's alleged schemes is unclear. The same goes for U.S. and Japanese regulators. Bank President Fujita dispatched his top international executive, Managing Director Hiroyuki Yan-



"If they can't control trading even in simple instruments, how about the more complex ones?" asks one law professor

JUDGE JAMES FRANCIS IV, DAIWA'S IGUCHI, AND LAWYER LEONARD JOY

rumpled blue jeans and rainbow-striped sweater, with masterminding a huge financial fraud. Iguchi allegedly covered up \$1.1 billion in losses from Treasury-bond deals by dipping into Daiwa customer accounts and doctoring paperwork to hide his trail. All told, U.S. Attorney Mary Jo White charges that Iguchi made 30,000 unauthorized bond trades, an "astronomical" amount. Iguchi, who has been fired, was arrested at his \$330,000 home in Kinnelon, N.J., on Sept. 23. He has not entered a plea and his attorney declined comment.

The Daiwa mess is a disturbing sequel to the February crash of Britain's Barings PLC, done in by Singapore-based trader Nicholas W. Leeson's \$1.4 billion loss on Nikkei index futures contracts.

thousands of miles away. That is forcing many financial executives to tighten scrutiny of trading desks—something prosecutors and analysts contend Daiwa should have done long ago. "Here," says White, "we appear not to have had any meaningful controls."

Daiwa's managerial shortfall is yet another stroke of bad news for Japanese lenders already burdened with an estimated \$800 billion in bad debts. Unnerved by several credit-union collapses and Japan's first postwar bank failure, investors now are demanding that big banks pay a premium to borrow in global money markets. With rating agencies considering a downgrade of Daiwa's credit standing, that premium now may widen. The Daiwa scandal is also

ji, to New York after he received the trader's written confession. Once he arrived, Yamaji and other Daiwa executives initially sent signals to Iguchi, who also had run Daiwa's securities custody department, that his career might survive if he cooperated. But Daiwa did not tell the Ministry of Finance of a problem until Sept. 18. Fearful that news of the loss would unsettle international markets, the ministry and Bank of Japan informed the Federal Reserve and other

major central banks. That prompted the Fed, which had been given increased power to regulate foreign lenders after the Bank of Credit & Commerce International collapse, to ask the Federal Reserve Bureau of Investigation to move on Iguchi.

In the wake of Iguchi's arrest, preventing billion-dollar trading catastrophes will now have to become an even more pressing concern of regulators and managers alike. Inevitably, some traders will slip through the net their overseers attempt to cast. But detecting financial fraud will have to take top priority. If it doesn't, the next accident on Wall Street could send pillars of finance toppling in places you'd least expect.

By Brian Bremner in Tokyo and William Glasgall in New York

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| Environmental Services    | 06-29-89 | 14.35  | -0.21  | 4.10  |
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| Industrial Materials      | 09-29-86 | 10.10  | 13.89  | 11.26 |
| Paper and Forest Products | 06-30-86 | 35.83  | 17.54  | 12.37 |
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| Precious Metals & Minerals               | 07-14-81 | -0.85 | 7.97  | 6.37*  |
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| Electronics             | 07-29-85 | 75.48  | 26.34  | 13.17  |
| Software/Computer Svcs. | 07-29-85 | 63.65  | 23.14  | 19.07  |
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## A DRUG SCANDAL MAY TAKE THE GLOW OFF COLOMBIA'S ECONOMY

Colombia's democratic tradition was put to the test on Sept. 26, when President Ernesto Samper Pizano was grilled for more than eight hours by a congressional committee investigating charges that his 1994 campaign took \$6 million from drug lords. That wasn't enough to rattle a multinational executive on the other side of Bogotá. Pulling out new flip charts for an upcoming presentation to New York bankers, he raved about Colombia's fast-growing economy and his company's expansion plans. "The big investors realize the two best places to be in Latin America these days are Chile and Colombia," he said.

To the outside world, Colombia is the land of cocaine and lawlessness. Indeed, the enthusiastic executive got a call just that morning from a guerrilla leader demanding money to "protect" one of the company's rural installations. But few outsiders realize that Colombia also has enjoyed a stable democracy for four decades and boasts an enviable economic track record.

**DARK SIDE.** Thanks to recent oil discoveries and to former President César Gaviria Trujillo's opening of the nation's markets, annual foreign direct investment nearly quadrupled over just two years, to \$4.6 billion in 1994. That above-board investment, plus an estimated \$1 billion a year in drug money, has produced economic growth averaging 4.2% over the past five years, peaking at 5.7% last year.

But now, Colombia's dark side is threatening its economic prosperity. Samper is increasingly on the defensive. He dismisses the charges against his campaign as slander and innuendo. But he has been hurt by the recent arrest of three of his top campaign aides, including Defense Minister Fernando Botero. So far police have seized cancelled checks showing the campaign received funds from traffickers' front companies, but if concrete evidence is found that Samper was personally involved, he could be forced from office.

Samper's problems are already shaking the heretofore sound economy. The peso has plummeted 9% against the dollar over the past month. Two Colombian banks that bet on the peso are reported to have suffered more than \$100 million in exchange losses. But not all the economic news is bad. The economy still expected to grow by at least 4.5% this year. And recent Moody's Investors Service shrugged off the Samper fiasco and upgraded Colombia's sovereign debt rating to investment grade—the only Latin American country except Chile to receive such a rating.

But if the uncertainty continues much longer there could be more serious consequences. One worry is that Samper could go on a spending spree to bolster his support. "If it's a short-term crisis, our institutions can handle it," says Miguel Largacha Martínez, vice-president of Banco Ganadero. "But the sooner this is solved, the better for the economy."

The Colombian Congress is expected to reach a decision by the end of October as to whether to recommend Samper's impeachment. It is far from clear what they will do. One factor: Drug traffickers are believed to have substantial influence over congress. In a sign of the turmoil that this crisis could produce, unidentified gunmen ambushed Samper's attorney the day after he testified, wounding the lawyer and killing two bodyguards.

Ironically, Samper's weakness has played into the hands of the U.S., which has been able to pressure him to go along with efforts to destroy coca and poppy plantations and imprison one of the seven main Cali kingpins, including Gilberto Rodríguez Orejuela. Those developments bode well for Colombia's efforts to shake its drug dependency. But first, Samper must either clear his name or leave the scene.

*By Geri Smith in Bogotá, Colombia  
with Stan Crock in Washington*



**NABBED:** Cali drug cartel kingpin Gilberto Rodríguez

### GLOBAL WRAPUP

#### JOCKEYING FOR CASPIAN OIL

► The Clinton Administration is putting very heavy pressure on an oil consortium led by Amoco and British Petroleum to use pipeline routes that pass through the territories of both Georgia and Russia to handle the shipments from a \$7 billion project in the Caspian Sea. Washington is worried that using only Russia would give Moscow too much future control over the vast oil reserves in the former Soviet republics near the Caspian. The decision on routes is expected to be made sometime in early October.

Members of the consortium, however, are concerned that the dual-route option could wind up costing up to \$600 million—too much to justify the relatively small volume of so-called early oil from the Caspian project. That oil is supposed to build confidence and help finance consortium operations and a future major \$1.5 billion pipeline. Beyond that, Russia has effective hegemony over Georgia, so it could easily interfere with oil going through the republic.

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## POLICY

# HOW LOW SHOULD RATES BE?

Taylor's Rule says lower, but the Fed is now ignoring it

Throughout his eight-year tenure as Federal Reserve Chairman, Alan Greenspan has kept Wall Street perpetually guessing about the future course of monetary policy. And for good reason. Rather than relying on a single indicator for changing interest rates, such as the money-supply figures Fed Chairman Paul A. Volcker claimed to follow in the 1980s, Greenspan has opted for an eclectic approach. He pores over hundreds of statistical and anecdotal factoids before determining where to set rates.

Now, some Fed watchers believe they have discovered a monetary crystal ball that could help them anticipate Greenspan's moves. The creation of John B. Taylor, a respected Stanford University economist and member of the Council of Economic Advisors under President George Bush, this forecasting tool has proven surprisingly accurate at predicting rate changes by the Greenspan Fed over the past eight years—at least up to now (chart). Over the past year, there has been a divergence between the actual Fed funds rate, now at 5.75%, and the predicted values. But if followers of Taylor's Rule are right about its predictive powers, it could portend further rate cuts by Greenspan that send the Fed funds rate below 5%.

**EARLY SIGN.** Taylor's Rule is a relatively simple formula that uses current growth and inflation to determine the optimal level of short-term interest rates. How good is it? Had Wall Street traders heeded Taylor's Rule, they would have anticipated critical turns in Fed policy, such as the February, 1994,



decision to raise the short-term Fed funds rate for the first time in nearly five years. Even those Fed watchers who had been expecting the policy reversal admit that Taylor's Rule would have helped them forecast the magnitude of looming rate hikes. Economists at Salomon Brothers Inc. figured that the Fed funds rate—the Fed's target price for overnight loans between banks—would only climb from 3% to 4.5%. But the rule predicted it would top out at 5.5%, which wasn't far off the actual 6% peak. "It really did come through," marvels Salomon economist Robert V. DiClemente.

Some economists believe Taylor's Rule works well because it perfectly captures the chairman's gradualist nature and his inclination to begin adjusting policy in advance of turns in the economy. Taylor's Rule "captures beautifully the considerations that the Fed looks at,"

says Northwestern University economist Martin Eichenbaum. Taylor claims that he didn't set out to predict Greenspan's moves on rates, but only to create a formula that would serve as a guiding principle for setting monetary policy. "The intent was to develop a good operating rule," adds Taylor. "The fact it came out so close was a surprise to me."

Just what are the ingredients in Taylor's formula? It states that the Fed funds rate should be determined by a formula based on actual inflation, the targeted level of inflation that the Fed hopes to achieve (which Taylor pegs at 2%), and the estimated size of the "output gap," which measures how far the economy is above or below its full-employment level.

Taylor's admirers say the rule succeeds because it focuses on whether the economy is operating above or below

## SEER

"The intent was to develop a good operating rule. That it came out so close was a surprise to me," says Taylor

its capabilities. If the economy is growing well below 2.5%, Taylor's dictum would tell the Fed how much needs to cut rates. Conversely, when the economy is growing above capacity, the rule advises the Fed when to begin applying the brakes and how hard to hit them. "The 'output gap' is

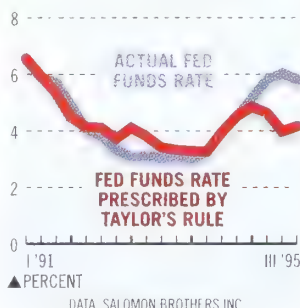
good proxy for determining how much slack the economy has and whether inflation pressures are building," says DiClemente.

**PARTING COMPANY.** Some Fed policy makers admit that they pay attention to Taylor's Rule. "It's a very good reality check," says Fed Governor Lawrence B. Lindsey. But for the most part, Fed officials consider it unwise to tether policy to a single operating rule. "Eclecticism has served us well" ever since money-supply figures became unreliable economic indicators, says Robert I.

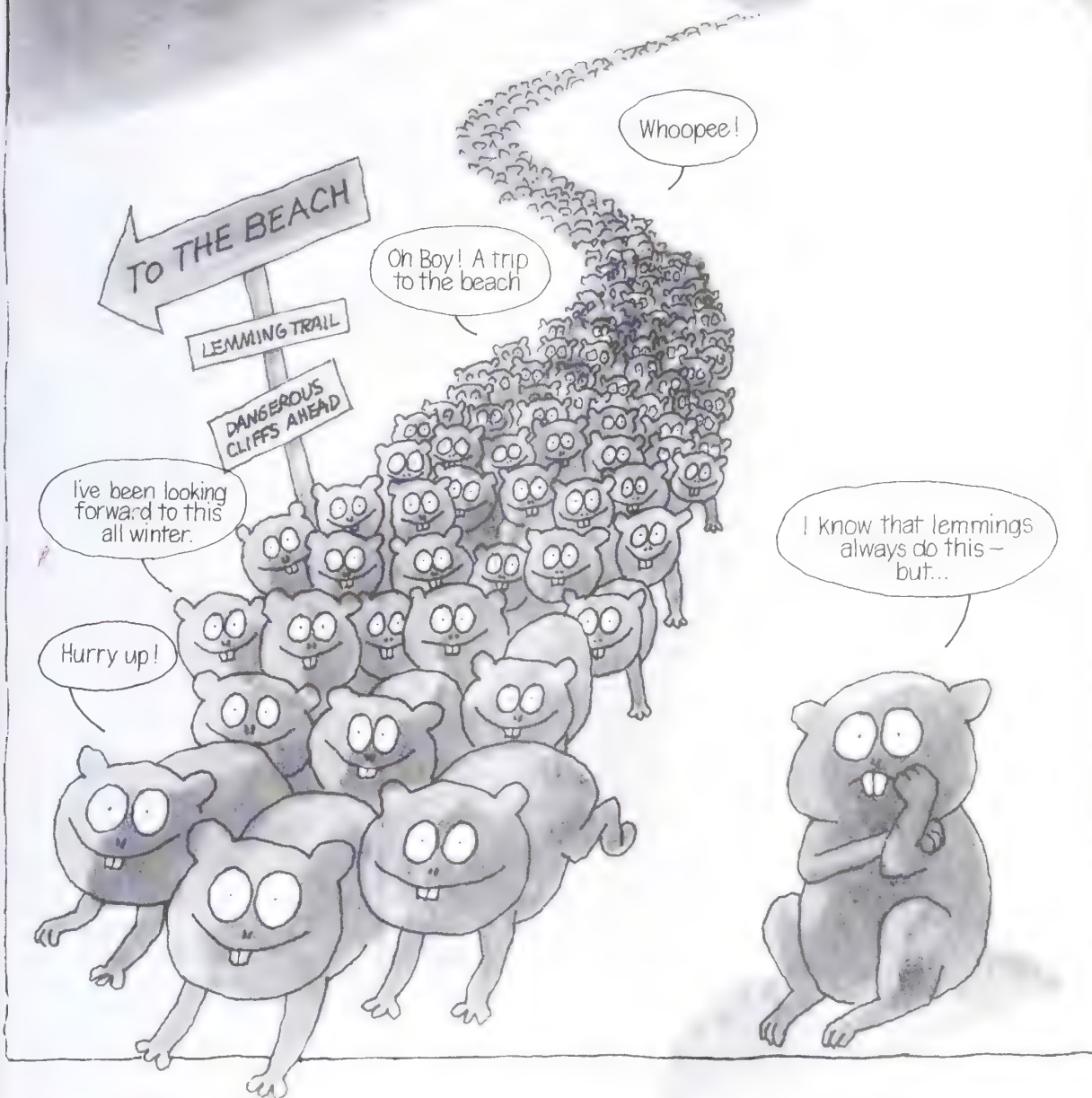
McTeer Jr., president of the Federal Reserve Bank of Dallas. "I don't pay attention to it. I don't say anything about other important considerations, such as the health of the banking system."

Indeed, starting last winter, Greenspan parted company with Taylor's Rule for the first time. The rule called for the central bank to b

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## Economics

gin easing the Fed funds rate toward 4.25%, but the central bank instead hiked rates as high as 6% to brake a surprisingly robust economy. Even now the Fed is reluctant to cut rates further. It took a pass at a Sept. 26 meeting. Fed officials say they're waiting to see if the White House and Congress keep their vow to slash the federal deficit. Then the Fed might cut rates more aggressively.

In retrospect, some economists blame Greenspan's failure to heed Taylor's Rule for the abrupt slowdown in the economy last spring. "February's hike was unnecessary, and one could argue that last November's rate hike was unnecessary as well," says Norwest Corp. economist Sung Won Sohn. Sohn now worries that short-term rates adjusted for inflation are too high by past standards, and he's urging Greenspan to get back in sync with Taylor's Rule—which tries to maintain real rates of 2% during a normal economy. "Every time the Fed funds rate exceeded the historical rate, the economy has gone into recession," he says. "This is a warning that the rate is too high and might hurt the economy in '96."

**AUTOMATIC PILOT?** Taylor himself is somewhat more cautious about how closely the Fed should follow his rule. "Cutting rates another 25 to 50 basis points would be reasonable at this point," says Taylor. He notes the Fed should always leave itself enough flexibility to respond to market shocks such as the 1987 stock market crash, which prompted the Fed to pump liquidity into the financial system, or the banking crisis of the early 1990s, when rates were kept low to help troubled banks repair their balance sheet. "I don't know if anyone who thinks we should turn the Fed over to a computer," agrees Eichenbaum.

That's not to say that the Fed could not use some help in calibrating monetary policy. Some economists see Taylor's formula as a starting point that would force Fed officials to justify the reasoning for deviating from it. "It's a good touchstone that would provide discipline to Fed thinking about the course of monetary policy," says University of California at Berkeley economist James A. Wilcox. "It would be healthy if the Federal Reserve tried to explain why it's a point above Taylor's Rule, even if it did so privately." With the economy still struggling to regain its legs after stumbling last spring, it may indeed be time for Greenspan to give heed to Taylor's Rule.

By Dean Foust in Washington

**HOT**

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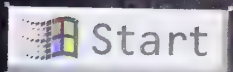


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# SECRETS OF THE SURVIVORS

Big-league tips from Lasorda, Shula, and Anderson

**S**ports trivia: Who first said, "Winning isn't everything, it's the only thing?" No, not Vince Lombardi. Try University of California at Los Angeles coach Red Sanders in 1953. Nonetheless, the sentiment still rings true: Win, or else. Ask any head coach.

Granted, few sports-team owners are as fickle or demanding as the New York Yankees' George Steinbrenner: He has swapped managers 21 times since taking over in 1973. Still, canning the head coach remains an acceptable management strategy. Although stats are hard to come by, there's probably no U.S. industry with a higher turnover rate for top management than major league sports: basketball, baseball, football, and hockey. Because these 113 head coaches and managers must contend with constant public scrutiny, extraordinarily well-paid employees, and often unrealistic expectations from their superiors, they operate under intense pressure.

Three coaches have managed to hang on to their current jobs far longer than all the rest: authoritarian Don Shula (Miami Dolphins head coach since Feb. 18, 1970), jovial Tommy Lasorda (Los Angeles Dodgers manager since Sept. 29, 1976), and the avuncular Sparky Anderson (Detroit Tigers manager since June 12, 1979). Coming in a distant fourth and fifth in the longevity sweepstakes, according to Elias Sports Bureau, are the Pittsburgh Pirates' Jim Leyland (Nov. 20, 1985) and Jim Mora of the New Orleans Saints (Jan. 28, 1986).

BUSINESS WEEK tracked down Lasorda, Shula, and Anderson to seek their management advice for the brass at other businesses.

*Two hours before game time, Lasorda leans back with his hands behind his head and his bare feet crossed on the corner of a desk in Shea Stadium's visitors' locker room. He's in his underwear and a faded blue Dodgers T-shirt. The Colorado Rockies have won two straight to crawl within a game of the*

*division-leading Dodgers, but Lasorda, 68, appears unconcerned. He's holding forth for a crowd of journalists and buddies. His ramblings today include tidbits about his marinara sauce, Michael Jackson's divorce rumors, Phil Rizzuto leaving his TV job, and Mickey Mantle's funeral.*

**Q:** What advice would you give to CEOs on handling pressure?

**A:** "Pressure" is a word that is misused in our vocabulary. When you start thinking of pressure, it's because you've started to think of failure.

Let's say we're playing the Yankees in game seven of the World Series, and we're up 3-2. Billy Russell is playing shortstop and Orel Hersher is pitching. The shortstop says, "If the guy hits the ball to me, we're going to lose." That is feeling the pressure. But if he goes to the pitcher and says, "Make him hit it to me because I'm going to get him out," now he is thinking of succeeding. Self-confidence is the first key to success.

**Q:** What makes a good manager or, say, a good CEO?

**A:** Managing is like holding a dove in your hand. If you squeeze too tight, you kill it. Open your hand too much, you let it go. That's the way it is with the players.

Solomon said the greatest gift you can give is an understanding heart. When a guy pops up with two men on and two out, and you're down by one and lose, I'm very upset. But you have to understand that guy is even more upset.

As a manager, I don't hit, catch, or throw for them. My responsibility is to



## TOMMY LASORDA

"Managing is like holding a dove. . . . Squeeze too tight, you kill it. Open your hand too much, you let it go"

get my 25 guys playing for the name on the front of their shirt and not the one on the back. But you have to understand the personalities.

**Q:** How do you judge a good manager?

**A:** I ask if he's getting the best effort out of them. Do they play with an unselfish attitude? That holds for managing a baseball team or managing a company with 50 people. I would run that job

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the same way. I wouldn't do anything f—' different. I would not only get to know the player, I would get to know his family.

**Q:** How do you mediate between upper management and your players?

**A:** You have to know the strengths and weaknesses of your players. To be successful, you need three things: good ballplayers, great communication with your players, and the support of the front office.

**Q:** With such talent around you, how do you balance egos with playing time?

**A:** I remember a player that said, "Why aren't I playing?" When I tell him about his deficiencies, I'm knocking him down. Which means when I gotta put him in the lineup the next day, I gotta build his confidence again. You have to make them feel like part of the ball club....

Don Shula, 65, is in his 26th season as head coach of the Dolphins. Along the way, he has amassed more total victories than any other coach in National Football League history (341) and has taken the Dolphins to a record five Super Bowls. Last year's 10-6 mark was



good enough to earn the Dolphins their 15th trip to the playoffs under his guiding hand. Sure, Shula hasn't appeared in a Super Bowl since the Dolphins got mauled 38-16 by the San Francisco 49ers a decade ago. And it has been almost 25 years since he guided the Dolphins through the only undefeated season (17-0) in pro football history. But, true to form, his Dolphins are off to a 3-0 start this year.

## DON SHULA

"You can't get away from the basics. Many times you get away from what you know—that's when you don't do well"

**Q:** What traits are needed to be an effective leader?

**A:** To be effective, as CEO or coach, you have to have credibility and communication. If players question what you say or how you act, you're going to have tough times. You've got to keep open ended communications at all times to go over problems and hold a team together.

**Q:** When things are going badly, what

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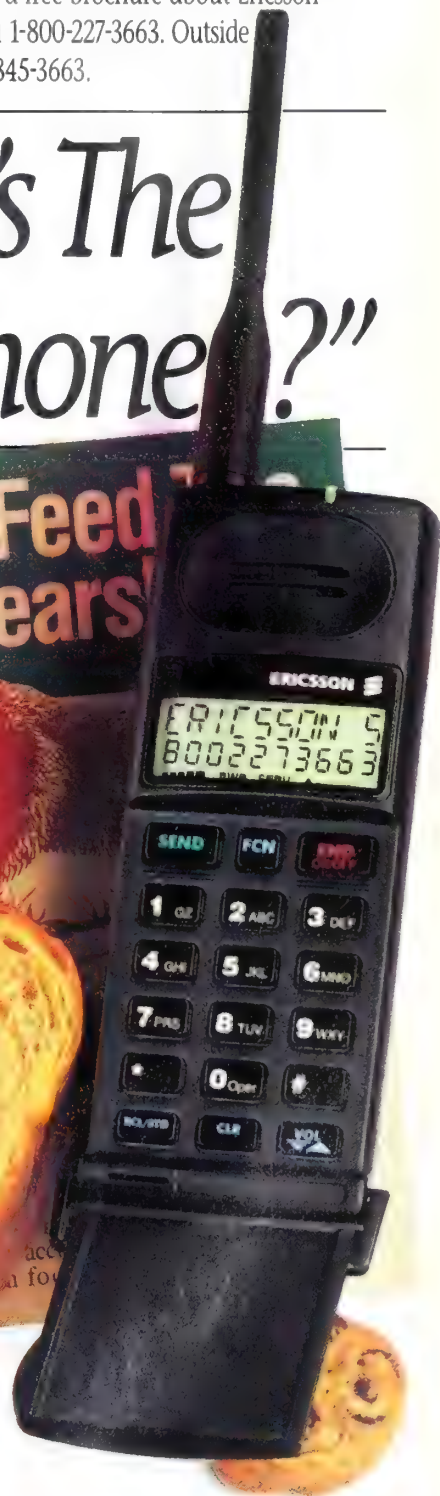
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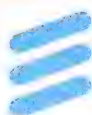
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**ERICSSON** 



advice do you have for CEOs about how to react?

**A:** You need to have your convictions. There's no magic formula. You can't get away from the basics. Many times you get away from what you know—that's when you don't do well.

**Q:** How do you fire somebody?

**A:** I believe in the straight-up approach. The toughest part of my job is having to tell a guy who's contributed to our success that he's no longer needed. They may not like it at the time, but they'll end up respecting you for it in the long run.

**Q:** How do you motivate highly paid, top-level athletes?

**A:** We don't talk much about money, what guys are making. It's pretty private. We just have our practices, our regimen. They know what's expected of them.

**Q:** What advice do you have for dealing with employees who create problems?

**A:** I make a decision that we're going to solve whatever it is, and then go in that direction. I've given many players second and third chances. I've lost some, and I've won some. I traded for Irving Fryar, [who] had a questionable reputation at New England. But he's been one of our team leaders, made the Pro Bowl the last two years.

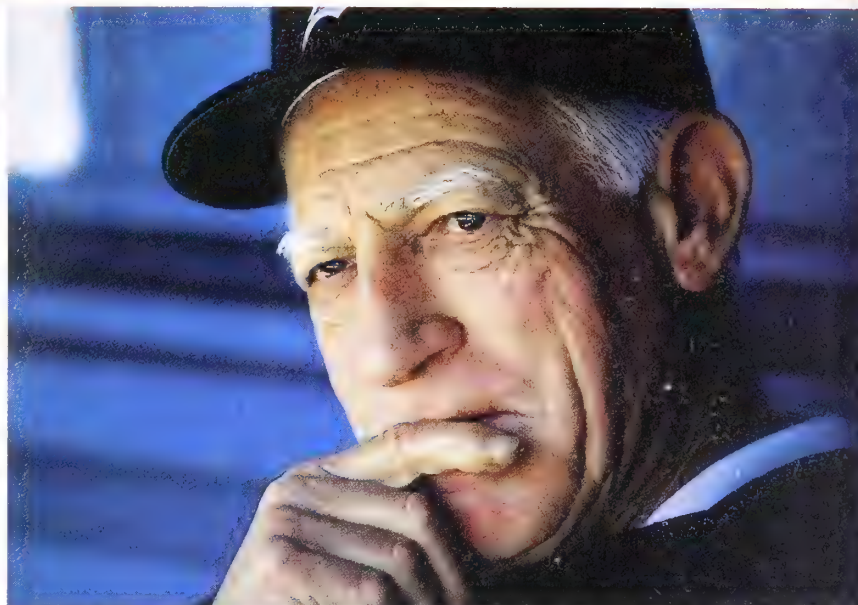
**Q:** How do you dole out criticism or praise to manage most effectively?

**A:** It's up to the individual. Some guys need a pat on the back and some guys need some public criticism. It's not the same for everybody. Everybody's got a different makeup.

**Q:** What's your No. 1 advice to CEOs?

**A:** You've got to have integrity to be an effective leader. That's what it all stems from.

The Detroit Tigers have won four straight in late June and are in second place, just four games behind the Boston Red Sox in the American League's Eastern Division. Sparky Anderson, 61, who has intimated that he may not be back next year, is smoking his trademark pipe (1926-brand tobacco) in the visitors' clubhouse at Yankee Stadium. He's wearing a white baseball undershirt with blue sleeves, game pants, socks, and slippers. In less than three hours, his team will open a crucial three-game series with the third-place Yankees. Anderson, a self-professed man of tradition, is explaining to the Tigers' beat



writers that even if game times are long, there's no place for a clock in baseball: "I don't want to know what time it is. I want to know what my ballplayers are doing."

**Q:** How have you managed to stay in your job so long?

**A:** Those that worry about getting fired know in their heart that they can't do the job. I never worried about keeping my job.

Those that get fired are the ones that can't deal with it. [Picks up the phone.] Call me and fire me. I'll find a job tomorrow. That's the only attitude you can have.

**Q:** How do you motivate guys who play for you?

**A:** You don't change. I can't change myself to motivate every guy who plays for me. You are who you are. If I try to figure out a way to motivate some guy, then I'm making up something that isn't me. I don't plan anything. When I start to talk, I just say whatever comes to mind and trust my instincts.

**Q:** You make your mistakes live in front of thousands of people, and they're broadcast on national TV. How do you react to mistakes?

**A:** I love to make mistakes. How are you going to become a ballplayer unless you make mistakes? I've made more mistakes than I've done things

## SPARKY ANDERSON

"Those that worry about getting fired know in their heart that they can't do the job. I never worried...."

right. But then they're gone. Over.

**Q:** What one piece of advice would you give to a CEO about to take over a company for the first time?

**A:** Never tell a lie. Always be yourself. That's it. Once you tell your first lie, you're done.

**Q:** How do you avoid burnout in this high stress, high-turnover environment?

**A:** Nobody can handle it. [Someone is] lying if he tells you he handles stress well.

**Q:** What other advice do you have for the CEOs of the U.S.?

**A:** Don't go brown-nosing, 'cause it catches up with you. Biggest trouble I see guys getting into is when they try to get in with the right side and the right people. They play both ends, and whichever end has the most power, they latch on with them. Be straight up.

**Q:** What makes a good manager?

**A:** The most overrated idea I hear is who can and can't manage. Nobody knows. But you can't learn to manage by copying. Take Don Shula. He's the greatest coach. Shula is Shula. It's his way. It's not your way or my way. You've got to do it your own way.

By Willy Stern and Elias Levenson in New York

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- 4 to 32 90MHz or 133MHz Intel Pentium processors per processor subsystem (node)
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- 4 MB second-level cache per processor
- 32 MB Limited Address Range Cache per processor board
- 64 MB-4 GB ECC type memory per processor subsystem
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- Redundant power supplies
- Optional redundant battery backup
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## AT&T WorldMark 5100C Cluster Configuration

- Clustering of 2 to 8 processor subsystems
- 1 or 2 processor subsystems per 5100C cabinet
- 4 to 32 90MHz or 133MHz Intel Pentium processors per processor subsystem
- Upgradable to next generation Intel processor family (P6)
- 4 MB second-level cache per processor
- 32 MB Limited Address Range Cache per processor board
- 64 MB-4 GB ECC memory per processor subsystem
- 16 I/O slots per node, 32-bit bus width per slot
- Up to 7 LAN and 24 WAN connections per processor subsystem
- Internal uninterruptible power
- Hot pluggable disk drives and fans
- Redundant power supplies
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- 4 to 32 133MHz Intel Pentium processors per processor subsystem
- Upgradable to next generation Intel processor family (P6)
- 4 MB second-level cache per processor
- 32 MB Limited Address Range Cache per processor board
- 64 MB-4 GB ECC memory per processor subsystem
- 16 I/O slots per processor subsystem; 32-bit bus width per slot
- Up to 7 LAN and 24 WAN connections per processor subsystem
- Internal uninterruptible power
- Hot pluggable disk drives and fans
- Redundant power supplies and battery backup
- Administration Workstation Subsystem (AWS) allows a single operation view of the entire system

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**MASSIE & SALISBURY:** The pair "have to grow quickly or get steamrolled"

## VIRTUAL REALITY

# CALL IT PALPABLE PROGRESS

The Phantom simulates touch—but will it make money?

**D**r. Thomas M. Krummel, chairman of the department of surgery at Penn State Medical College, slowly guided a biopsy needle into a small, hollow cone pressed against a wall. Pushing the needle in, he hit resistance, followed by a gentle pop as he pierced the outer skull. A second, harder pop told him he had penetrated the inner skull. The needle then slid easily through two inches of soft brain tissue and stopped. Probing gently, Krummel felt a solid mass: a tumor. One firm poke, and he was inside it.

This "operation" took place last fall. But there was no blood or brain tissue, or even a patient. Instead, Krummel was using one of the most advanced interfaces yet developed for a personal computer. The brain tumor was an image on a computer screen. The needle was a thimble on the end of his finger, held in place by a robotic arm. Through the thimble, Krummel controlled the needle on the screen, and "felt" resistance thanks to three motors guiding the thimble's response. "The accuracy is excellent," says Krummel. "It's truly awesome."

## THE BENEFITS OF TOUCH

Although still a prototype, SensAble Devices' Phantom offers a glimpse of what force-feedback can do for science and industry

**BIOLOGY** At the University of North Carolina, scientists use the Phantom to handle models of experimental drugs and sense how they might fit into a virus to inhibit it.

**AUTOS AND DEFENSE** Chrysler may use the Phantom to let engineers run their hands over virtual buttons and dials. GTE uses it to mock up radar control panels.

**ENTERTAINMENT** SensAble wants to adapt the Phantom as a game joystick that can reproduce vibrations of a tank on rough terrain or the feeling of opening a trapdoor.

The object of Krummel's praise is a desktop system called the Phantom. Although still a prototype, it represents a technological leap forward for the field of virtual reality. That's because, compared with mind-bending 3-D illusions from companies such as Silicon Graphics Inc., the technology to simulate touch—known as "force feedback"—is in its infancy. Scientists and product designers crave this tactile dimension, to enhance their engineering simulations (table). And though rival systems exist, the Phantom is the most flexible and economical. "This is a real breakthrough," says Professor Patrick H. Winston, the head of Massachusetts Institute of Technology's Artificial Intelligence Lab, where the Phantom was invented.

**INSTANT SENSATION.** The Phantom's simplicity springs from necessity. Thomas H. Massie, 24, built the first version in a rush, for his senior thesis project at MIT in 1993. The idea came from his adviser, J. Kenneth Salisbury, a principal research scientist at the AI lab. Together, the two applied for a patent and formed SensAble Devices Inc. in Cambridge, Mass.

The Phantom was an instant sensation among robotics and computer control mavens. Despite its crude appearance—the system had exposed wires running along the robotic arm, and a container the size of a lunchbox for the circuit boards—orders began to flood in. Over the next year, SensAble sold 40 Phantoms to some of America's top virtual reality labs.

The two inventors have plenty of competition. Force-feedback devices have been around since the 1970s, when the Atomic Energy Commission began using remote-control robots to handle radioactive materials. These systems were expensive and highly specialized. But lately, other small companies have rushed in. Cybernet Systems Corp., based in Ann Arbor, Mich., and Immersion Corp. in Santa Clara, Calif., both have PC-based force-feedback systems.

Still, the Phantom's growing ranks of supporters say that for just under \$20,000, SensAble's design offers the



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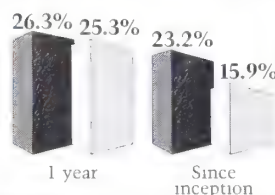
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best tactile response. "What's special about this," says John Armstrong, a former vice-president for science and technology at IBM, "is that it's small and handy and will adapt to any number of uses." Adds John Latta, president of high-tech consulting firm 4th Wave Inc. in Alexandria, Va.: "No one has been as good at tactile feedback."

The technology behind the Phantom is integrally linked to advances in low cost computing power, according to Salisbury. The system runs on a fast Intel Pentium processor. It allows designers to write software that simultaneously processes signals from motion sensors on the Phantom's arm and sends instructions back to the motors, telling them how much pressure to apply to the thimbles. The whole digital relay race repeats 1,000 times each second making the Phantom sensitive to the subtlest hand motions.

**PRIZE PUPIL.** Constructing such system is nothing new for Massie. As a ninth grader in Vanceboro, Ky., he built a computer-activated robotic arm and won second prize in an international science fair. Earlier this year, MIT gave him its most prestigious prize for invention.

Next, he'll have to make Phantom perform in the marketplace. The product is still too rough for mass production. And even some techies in SensAble's camp, such as Marc H. Raibert, president of virtual reality consultant Boston Dynamics Inc., says the Phantom can be "difficult to program." Worse, the window of opportunity could be closing. While Massie talks about turning the Phantom into a \$200 joystick for the computer-game market, rival Exo Corp., in Waltham, Mass., may be ready to ship such a product next year.

To whip the operation into shape Massie and Salisbury hired former IBM finance and marketing manager Bill Aulet as president in July. Aulet hopes to raise venture capital to expand production and to hire more programmers. Initially, he says, SensAble will target surgeons, who could use the Phantom to rehearse procedures before actually raising their scalpels. Aulet is also working on a software "toolkit" to help user design their own applications.

If he can keep these programs on track, Massie thinks the Phantom's superior performance will win customer loyalty and set a standard. "We're going to have to grow quickly or get steamrolled," Massie says. He has already demonstrated that force feedback can be a force in research labs. Now he has to show that it's ready for the mass market.

*By Geoffrey Smith in Boston*

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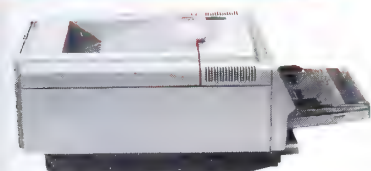
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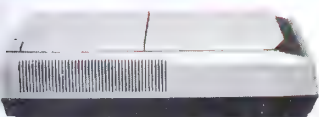
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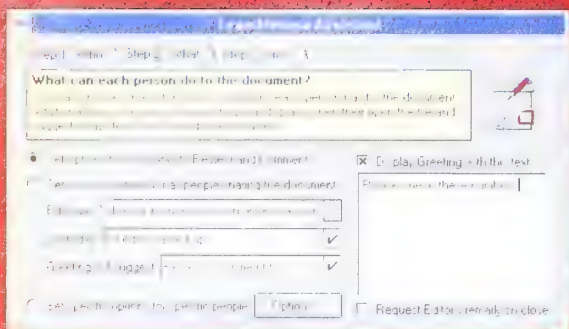
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September 30, 1995

Mr. and Mrs. Arthur Sweetser  
126 Squires Road  
Marco Island, Florida

ZIP?  
33969

Arthur's on vacation  
until Oct. 15 - date it  
+ send late that week.

Dear Arthur and Cindy,

I have reviewed your estate plan <sup>with Rebecca</sup> <sup>R</sup> as reflected in your present Wills and the schedule of assets that you left with me. My comments and suggestions follow.

recently

Your present Wills provide the desired flexibility to determine after the first death the amount of marital deduction to be utilized in order to achieve the best federal estate tax result. A problem arises, however, by reason of the way you presently hold <sup>COMBINED</sup> assets. In the event Arthur is the first to die, his two IRAs and Annuity would pass to pursuant to the beneficiary designations in place, leaving no assets with which to produce a taxable estate and utilize any of Arthur's available unified credit. While there will be no federal estate tax payable on Arthur's estate, the tax in Cindy's estate may well be higher than it needs to be by reason of the failure to use Arthur's unified credit.

attach  
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nation

Can we insert a table here?

To illustrate the foregoing, using the values contained on your Schedule of Assets, and assuming Arthur dies first and that Cindy dies one year later <sup>#</sup> with no change in asset values, <sup>≡</sup> arthur's gross estate for federal estate tax purposes would be \$580,007.00 representing the sum of the two IRA accounts and the annuity. Assuming no administration expenses, there would be a marital deduction taken in the amount of \$580,007.00 since each of the assets making up the gross estate pass to Cindy, producing a taxable estate of -0-. Upon Cindy's death, her gross estate for federal estate tax purposes will equal \$2,432,012.00, representing the sum of the above assets received for Arthur, the investment account, her IRA, the primary residence, and the New

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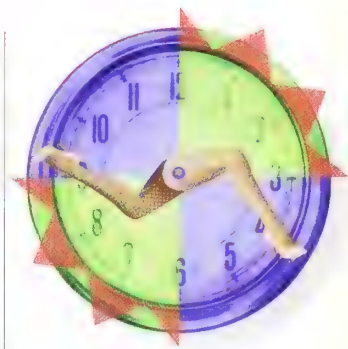
## PEPPING THE MAINPOWER CHINA

THE 1980S, WHEN JAPAN'S electronics giants were at the peak of their powers, U.S. officials fretted about American technology being siphoned to Asia through cross-border alliances and acquisitions. Now, the pendulum has swung back. Companies such as AT&T and Sun Microsystems Inc. are tapping Russia's wealth of physi-

cists and electrical engineers. And the scientific resources of China could be the next gold mine.

China-America Technology Corp., a new company that's 51% owned by City College of New York, wants to be the main facilitator in U.S.-China technology exchanges. CTC hopes to provide U.S. companies with information on technology and inventions emanating from the 50,000 scientists and technical staff of the Chinese Academy of Sciences and other key insti-

tutions. Soon, it will start mailing out bimonthly notices to subscribers—mainly large U.S. companies—who will pay varying rates, depending on the requested level of detail. Chinese Academy members include world-class physicists as well as specialists in ceramics, fermentation, and pollution control, says City College professor and CTC CEO Ngee-Pong Chang. And its members can draw on a tradition of plant-based medicine that stretches back several thousand years.



## INNOVATIONS

■ American women spend an estimated \$2 billion a year on panty hose. What's driving all that demand? Runs. Now, ELI Corp. in Northbrook, Ill., claims it has a solution: a 4-oz bottle called Forever Nylons—enough to treat 64 pair of hosiery—that sells for \$4.99. ELI says the liquid contains acrylic polymers that bond to nylon fibers, protecting them against runs.

■ What's killing the great trees of North America? Air pollution, says plant ecologist Orié Loucks at Miami University, Oxford, Ohio. Trees in the old-growth forests of the eastern U.S., stretching from Alabama to Pennsylvania, seem to be dying at three times the natural rate, he says. Some species, such as hickory, don't produce seeds until they are 150 years old. The hickory trees in these forests may not live long enough to reproduce.

## SELF-CLEANING WINDSHIELD? IT'S IN THE WORKS

DRIVERS ON LONG HAULS GET TIRED OF wiping through grimy windshields. Wipers help, but self-cleaning windshields could be better. They may be just around the corner, and chemical engineer Adam Heller says they should add more than \$100 to the cost of the car. His idea is to treat windshields with a thin, transparent film of titanium dioxide, which he developed with his colleagues at the University of Texas at Austin. When the sun's ultraviolet rays hit the coating, they trigger a chemical reaction that strips the glass of organic material, such as soot, tree sap, and oil.

Camera makers already coat

lenses with titanium dioxide to help them resist scratches. And scientists have long been aware of the compound's reactive power. But to make use of it on windshields, Heller and his colleague,

Yaron Paz, first had to purge the glass of sodium, which blocks photocatalysis. They did that by bathing the glass in acid. Now, they're ready to commercialize their results. Even if they succeed, titanium dioxide won't put car washes out of business. It only seems to work on layers of grime that build up slowly. Larger deposits, such as splattered insects and bird droppings, will still require wiping.



## MORE HORSEPOWER FOR YOUR CAR STEREO

THE NEXT TIME YOU THOUGHT CAR sound systems couldn't possibly get any louder, a radical advance in speaker design is threatening to shake the sidewalks in American cities. By March of next year, Phoenix Gold International Inc. of Portland, Ore., hopes to introduce a new species of subwoofer—a component in most high-end speaker systems that is optimized for bass. For around

\$700, Phoenix' 12-inch "Cyclone" unit will pump out about three times as much bass sound as other subwoofers with the same dimensions.

That's big news because traditionally, the only way to get more bass sound has been to build a bigger box. Subwoofers, which use the same 60-year-old technology as conventional speakers, achieve their powerful bot-

tom notes by means of a magnetic coil that moves back and forth along a linear path, punching out the sound waves as it goes. Since the range of movement is limited, creating more sound requires a longer path.

In contrast, the Cyclone's magnets are mounted on a round armature that twitches like the needle of a dial each time an electrical signal pulses through. These rotary magnets, invented by

Chicago-based Intersonics Technology Corp., are fitted with lightweight rectangular vanes made of polystyrene and carbon fiber. The vanes push more air around, and thus create more powerful waves. That's good news for road rockers: They won't have to surrender car trunk space to attain the big boom. If all goes well, Phoenix hopes to move the same technology into the \$150 million market for home-theater speakers.





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# UNISYS



## DEMOGRAPHICS

# THE BOONIES ARE BOOMING

Young and old are moving back to Smalltown, USA, and suddenly the sticks are a marketer's dream



**GLOBAL VILLAGER:** Abraham keeps his finger on the pulse via 14 phone lines

**W**hen Salem Abraham bid to handle part of Smith Barney Inc.'s derivatives portfolio, the New York brokerage firm was skeptical. After all, instead of working out of skyscraper offices in Manhattan or Chicago, Abraham does his trading from a three-story building in Canadian, Tex. (population 2,500), amid the loamy mesas two hours northeast of Amarillo. Abraham showed a Smith Barney manager who trekked to Canadian his two satellite dishes, his 14 lines for phones, fax, and modems, and his 11 personal computers. But what really sold her was a campfire dinner at his cattle ranch that night. As they chowed down on chicken-fried steak, the cellular phone in his pickup started to shrill: Japan's currency was falling, and Abraham's floor trader in Tokyo wanted to unload 1.5 billion yen. "We started trading right there by the campfire," recalls Abraham. Within a week, Smith Barney added its funds to Abraham's \$130 million under management.

Opportunity is on the line all over

rural America. The romance and solitude are still there, but they've been joined by technology and commerce that allow professionals and entrepreneurs of all stripes to ply their trades from the prairies, the mountains, and the forests. They're reversing decades of migration, boosting rural wealth, and bringing new spending power, development, and opportunities to the American hinterlands. Indeed, since 1988, job growth in nonmetropolitan areas has outpaced that in metro areas. Counties in vacation or retirement areas or ones that have strong technology infrastructures are leading the way in growth.

Marketers, who long shunned the backroads, have seen the changes and are going country in

droves. Consider Timothy F. Finley. For two years, the CEO of Joseph A. Bank Clothiers Inc. resisted a letter-writing campaign from tiny Quincy, Ill., to open a Bank franchise in the Mississippi River town. With a population of 40,000, Quincy was half the size of Bank's smallest market. But Finley gave in after delegation of civic leaders led by Mayor Charles W. Scholz flew to Baltimore to make their pitch. The result? In its first full year, the Quincy store will lo

## The Fastest-Growing Places You Never Heard Of

**INCOME GROWTH SINCE 1990** **POPULATION GROWTH SINCE 1990**

DATA: CLARITAS INC., COMMERCE DEPT., BUSINESS WEEK



**COLUMBIA, TEX.**  
Saturn plant  
nearby Spring

REASON ►





## Faxes, laptops, and modems allow professionals to ply their trades from the hills to the prairies

million in sales, 67% more than previous years. Finley has already cut ribbons for 10 new small-market bank stores and is considering a rollout to 56 more sites nationwide. "We're looking at it real hard," he says.

He's not the only one. Across town, Home Depot Inc. in July opened a new store of store called Crossroads. The company store and others like it in Columbia, Mo., and Waterloo, Iowa, offer a unified mix of do-it-yourself tools and materials, the first nonmetro ventures of the supersuccessful chain. Sears,

### GOING UP: *Chip plant in Harvard, Ill.*

Roebuck & Co. expects to have 800 rural stores open in five years.

Clothing, hardware, and appliances are just the start. From books to telephones, from credit cards to hotels, rural America is reaping a cornucopia of commerce. Outlet stores and catalog retailers, which long have catered to sobbusters and homemakers, are multiplying and reaching into new markets all across the country. In industries as diverse as health care, hotels, and telecommunications, entire businesses are growing up that focus exclusively on nonmetropolitan customers. Credit-card consultant Mike Auriemma says card issuers, who once shunned rural customers, now court them—and the

competition is heating up: "The attitude is going to be, 'Ready, shoot, aim.' You really have to move fast."

Why the land rush? Companies are going country because there are more rural residents, with more money to spend, than ever before. For the first time since the 1970s, problems such as crime, crowds, and high costs are driving urbanites out of the city faster than rural folks are replacing them. Indeed, migration into rural counties jumped 2.2% from 1990 to 1994, handily outpacing the 1.3% growth in migration to ur-

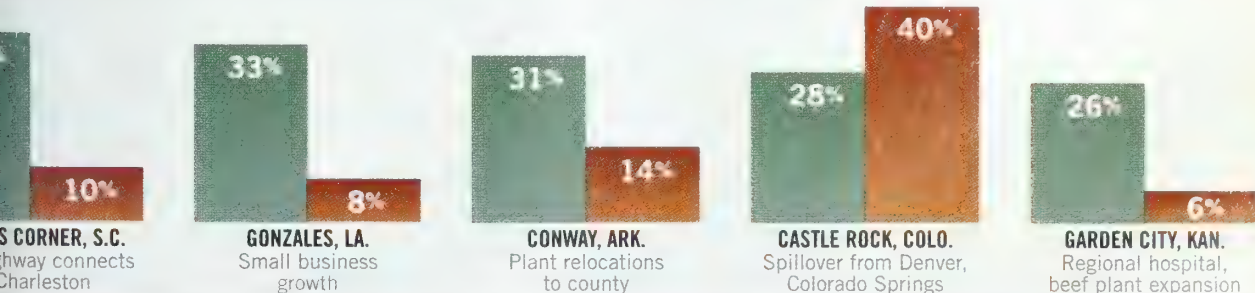
ban counties. Overall, rural counties have seen their populations grow at a 1% annual growth rate, triple the rate during the 1980s.

And it's not just people. Industries are migrating, too, drawn by cheap labor, cheap land, and ever improving technology. When a military base near Charleston, S.C., closed last year, some companies saw opportunity in the lower wages and falling real estate prices that resulted from the weakened economy. The region, with an educated work force, attracted a steel minimill, several high-technology businesses, and a new retirement community. Prisons and casinos—both growth industries—almost always locate in small towns where costs are low.

**LIFESTYLE LURE.** Once development starts, it can snowball. A big factory-outlet mall or retirement community plunked down in the boondocks soon attracts satellite businesses such as hotels, restaurants, and other retailers. Besides the savings companies reap when they set up outside costly urban centers, employees like the lifestyle. "There's a growing strand of anti-urbanism in a fairly significant part of the population," says Kenneth M. Johnson, a Loyola University of Chicago sociologist who studies population shifts. "People want to live and work outside the cities."

That's what led Bernie Zurbriggen to a small mountain town on the road from Denver to Vail. Zurbriggen spent 19 years working for phone companies in five different cities, but in 1990 he and his wife moved to Frisco, Colo. (population 1,900). Zurbriggen designed an automated *Blue Book*-type of service for used-car pricing that customers reach on a 900-number phone line and that he runs from home. "It's kind of a leading-edge, bleeding-edge business," Zurbriggen, 51, jokes about his \$400,000-a-year enterprise.

Rural residents today aren't the hicks and hayseeds of the Norman Rockwell era. Farmers and mine workers are now only 10% of the rural population. Not that the farmers aren't doing well: Few-





er farmers are plowing more land and making more money than ever. Farm income has set records in four of the last five years, and farm debt is at its lowest level since the early 1980s.

Add it all up, and there's a new prosperity in the 81% of the nation's land that lies in nonmetropolitan areas. In 1992, the nonmetro unemployment rate was lower than urban unemployment for the first time since before 1980, and it has stayed that way since. City dwellers still earn more money, but income for rural residents has jumped an average of 5.1% annually since 1990, outpacing urban income growth, at 4.8%, and reversing a 20-year trend. In 15 states, rural counties rank highest in per-capita income.

Not long ago, marketers were certain rural customers were too costly to reach, too tight with money, and too loyal to local businesses to be worth the effort. But that complacency was shattered when the Wal-Mart Stores Inc. juggernaut rolled through America's outback in the 1970s and '80s. Although many viewed Sam Walton's success as an anomaly, no one could deny he was reaping bumper profits from markets his competitors had scorned.

**FROM THE STICKS.** Then came the technology revolution. Suddenly, city folks sick of the rat race could pack up their PCs, fax modems, and cellular phones and plug in anywhere they wanted. Consultants, money managers, and other professionals could service clients as easily from the sticks as from their old urban canyons. Corporations, happy to cut down on office space, began to encourage telecommuting, allowing employees to live farther out from the headquarters hub. The ranks of teleworkers have catapulted from just under 2 million in 1988 to nearly 11 million today, according to LINK Resources Corp. Marketers have moved in right behind them. Mail Boxes Etc., for example, looks for small towns with lots of work-at-home business people who buy its mail and fax services.

At the same time, technology has made it easier for manufacturers to locate away from the urban centers. Motorola Inc. chose to put its new computer chip plant in Harvard, Ill., a farm town that boasts an outsize statue of a Holstein cow in its town square. Remote Eldorado Hills, Calif., 30 miles outside Sacramento, is home to two major employers thanks to high-powered data links. International Billing Service processes bills for utilities nationwide, while Fortune 800 provides 800-number telephone services.

To reach growing rural markets, companies now are more willing to absorb

## THE OLD BRING NEW LIFE TO BLUFFTON, S.C.

**B**luffton, S.C., in the lowlands of Beaufort county, doesn't look like much, but it has a rich history. The 15-foot-wide Secession Oak still stands where townsfolk met in 1844 to secede from the Union—years before South Carolina did. The Church of the Cross with its cypress timbers is still standing, even though Union troops torched the summer homes of planters on the nearby waterfront. The Bluffton Eagles semi-pro baseball team, many of them descendants of slaves and freedmen,

permanent tourists," says Governor David M. Beasley. "They're not going anywhere, and neither are these jobs."

Retirement living is fueling a lot of rural development today and, in the process, creating irresistible opportunities for marketers. Employment in retirement-destination counties, primarily in the Sunbelt, grew 3.7% last year, outpacing the 2.3% growth in metropolitan counties. And from 1990 to 1994, population in those counties jumped 10.7%, more than any other

category, says demographer Kenneth M. Johnson of Loyola University of Chicago. **MAIN CHANCE.** To see exactly what those numbers mean on the ground, check out the area surrounding the new Sun City. The impoverished lowlands region where the development is taking root was left untouched when the Hilton Head Island resort was built during the 1970s—just 20 miles away. But today, on the heels of



**SUN CITY DWELLERS:** *Retirees mean jobs*

the Sun City construction, paper company Union Camp is readying plans to build a shopping mall on timberland it owns nearby. And competing residential developers have also snatched up big tracts of land.

That's just the start. To bring water to Sun City, Webb sank a \$17 million, 8-mile-long water and sewer main, which will generate light industry construction for decades. The state is planning a new community college nearby. Indeed, development plans mushroomed so fast after the Sun City announcement that Beaufort County put a six-month moratorium on new construction so it could draw up a development plan. The Secession Oak, Church of the Cross, and Eagles Field are safe, but all bets are off on the rest of tiny Bluffton.

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*By David Greising  
in Bluffton, S.C.*



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One team, in CUSA Production's Western Business Unit, is tracking the profitability of individual wells. "It's a tremendously difficult task to optimize our field operations for maximum profitability," says Alameda.

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***Reaching for the Best***

Alameda looks forward to extending the use of the metrics and performance monitoring data to employees trying to improve their work processes. He admits

his vision is far reaching, but so is the SAS System. "Our challenge is to be better than the best," he concludes, "and the SAS System is helping us reach that goal."

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## Marketing



**TV PIONEER:** Larson was the first in Almont, N. D., to get a DirectTV dish

bigger distribution and advertising expenses. Take TDS Telecommunications Corp., a \$500 million company based in Madison, Wis. It spent \$80 million to build multimedia communications facilities so it could sell videoconferencing and other services to small businesses, schools, hospitals, and corporate outposts in its rural marketplace.

**LITTLE MACS.** Other marketers are narrowing their focus with sophisticated database marketing. Home Depot cross-cut a variety of databases when it was scouting Crossroads locations, including census trends, the number of farms and tractors, sales tax collections, and consumer credit. Its real estate experts flew to more than 180 small towns, where they counted traffic, talked to people in coffee shops, and read the local papers.

Marketers are taking their business to customers in new ways. As part of their pending merger, First Union Corp. and First Fidelity Bancorp expect to close some costly small-town branches in the Northeast. But they're hoping to keep the business by moving teller operations into grocery stores.

Even so, the rural market is hardly a can't-miss target. When McDonald's Corp. brought scaled-down restaurants into towns with just a few thousand residents, such as Machias, Me., it found that customers were so accus-

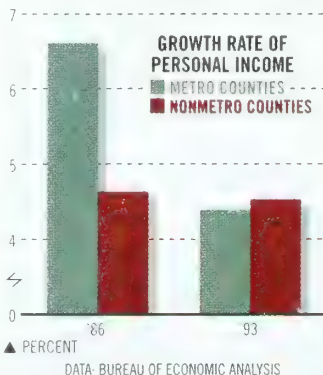
tomed to the full-size McDonald's they saw elsewhere that they shunned the miniaturized version. Machias still has its fast food, but McDonald's USA Chief Executive Edward H. Rensi says the chain will concentrate on urban markets, where it obtains 80% of its growth.

While rural population and income numbers may be up nationally, many rural towns remain pockets of deeply embedded poverty. In Shomokin, Pa., the textile mills have shut down, the jobs are gone, and no telecommuters or retirees are moving in. "As soon as our young people are out of school, they have to leave to find work," laments Ralph Victoriano, executive director of the Shomokin Chamber of Commerce.

Even markets that are thriving require skill and capital to penetrate. To day's rustics are familiar with high tech and are unwilling to settle for second best. Century Telephone Enterprise Inc., based in Monroe, La., finds a grow-

ing demand among its mostly rural customers for add-on services such as Caller ID. In response to a recent customer poll, Century soon will offer local access to CompuServe to customers in small towns such as LaCrosse, Wis., where computer users previously had to dial long distances to reach online services. "There's been a lot of talk about competition coming in," say

## Land Of Opportunity



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| <input type="checkbox"/> BUSINESS <input type="checkbox"/> HOME |  |  |  |  |  |  |  |  |  |           |  |  |  |  |  |  |  |  |  |
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|                                                                 |  |  |  |  |  |  |  |  |  | EXTENSION |  |  |  |  |  |  |  |  |  |
|                                                                 |  |  |  |  |  |  |  |  |  |           |  |  |  |  |  |  |  |  |  |

Please check one response for each following question.

What is your company's type of business?

- ☐ Agriculture  
 ☐ Mining, Construction  
 ☐ Manufacturing, Processing  
 ☐ Wholesale, Retail Trade  
 ☐ Finance, Insurance, Real Estate  
 ☐ Government  
 ☐ Transportation, Public Utilities  
 ☐ Service Industries  
 ☐ Other - Please Specify:

What is your title?

- ☐ Chairman of the Board  
 ☐ President  
 ☐ Vice President  
 ☐ Treasurer, Secretary  
 ☐ General Manager  
 ☐ Division Manager  
 ☐ Department Manager  
 ☐ Other Manager

Student ☐ Other - Please Specify:

How many employees in your company worldwide?

- ☐ Under 100  
 ☐ 100-999  
 ☐ 1,000-2499  
 ☐ 2,500 - 4,999  
 ☐ 5,000 - 9,999  
 ☐ 10,000 or more

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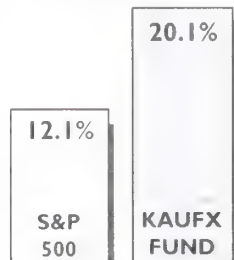
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*Mutual Funds Magazine, April '95*

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Total returns for periods ending June 30, 1995 are historical and include change in share price, reinvestment of dividends and capital gains. There is a 0.2% redemption fee and a 12b-1 fee in excess of 0.25%. The S&P is an unmanaged index consisting of the common stock of 500 publicly traded U.S. companies. For more complete information including charges, expenses, and risks on small-cap stocks please read the prospectus carefully before you invest. The performance cited represents past performance which is not indicative of future results; investment performance fluctuates; fund shares when redeemed may be worth more or less than original cost. The prices of small company stocks are generally more volatile than those of large companies.

## The Kaufmann Fund, Inc.

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See the Fund on the Internet at <http://networth.galt.com/kaufmann.09>

## Marketing

Post. "We don't plan to let them in, even if we have to pay for extra technology."

One of the biggest successes of DirectTV Inc., the pizza-size satellite dish that pulls high-quality digital television transmissions from the sky. The venture, developed by Hughes Electronics Corp., a unit of General Motors, and Thomson Consumer Electronics Inc. has drawn more than 800,000 paying subscribers in its first full year of operation, about half in rural areas. In Monticello County, N.D., cattle ranchers Jake and Virginia Larson made the front page of the local paper when they were the first in the area to get one. Today they watch plenty of sports and old movies, and their grandkids eyeball the Cartoon Network—none of which was available to them before DirectTV. Still, Jake isn't fully satisfied. "I wish there had more rodeos on," he complains. "People out here like rodeos."

**NEW CONCEPT.** It's no mean feat deciding what rural folks want and how to get it to them. Just ask Sears, which retreated from rural markets in early 1994 by shutting down its catalog-store operations. Just weeks after its exit, Sears was already mapping out a new rural offensive. It turned to a core of former catalog-store managers with a new concept: dealer stores. Sears owns the inventory and pays for advertising, while dealers cover leases, payroll, and other expenses and take home an undisclosed cut of sales. Often located within blocks of a major competitor like Wal-Mart or Kmart that can pull in customers, the new, bigger dealer stores are 6,000 square feet or more. The experiment works. Sears already is close to its original target of 350 locations, and the stores are ringing up yearly sales of about \$1.3 million apiece—30% over expectations. The Sears board just authorized an expansion to 800 sites by 1996. "We really have exceeded our expectations," says Steven L. Titus, vice-president for dealer stores.

Other marketers have also learned to piggyback on Wal-Mart and other giant competitors. Musicland Stores Co. locates its On Cue stores close to such behemoths, hoping to lure some of the customers with a better selection and more knowledgeable sales staff. "We're not a destination store," says Larry Kurzeka, general manager of On Cue. But if the town's household income averages nearly \$30,000, and 12,000 cars pass the location each day, chances are the On Cue store will succeed, he adds.

At Promus Hotel Corp., franchisees try to build the chain's miniversion of a value-oriented Hampton Inns chain.





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|-------------|----------------|
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*This announcement appears as a matter of record only.*

**\$252,714,000**

**TRUCK COMPONENTS INC.**

*has been sold to a wholly owned subsidiary of*

**JOHNSTOWN AMERICA  
INDUSTRIES, INC.**

*The undersigned acted as financial advisor to Truck Components Inc.  
in the sale to Johnstown America Industries, Inc.*



**CASTLE HARLAN, INC.**

October 1995

New York

**Marketing**

competitors' shadows. Promus is focusing on places such as Johnson City, Tenn., and Cape Girardeau, Mo.—towns with around 30,000 citizens located on major travel routes. "If you're building next to a tired, full-size, 150-room property of a competitor, you know you've got people looking for a hotel already," explains Tom Keltner, senior vice-president for development. Apparently, he's right: Occupancy rates run at 74%—about 10 points above the industry average and on a par with full-size Hampton Inns. Keltner says Promus franchisees recover their investments in the rural hotels in about a year, compared with three years for its standard hotels. Since the launch in 1991, Promus has opened 106 of the 60-room, small-market hotels—properties about half the size of normal Hampton. Nearly half the Hamptons built this year will be the smaller version.

**COUNTRY DOCS.** Even in the fast-changing world of health care, firms such as Health Management Associates and Community Care of America, based in Naples, Fla., are setting their sights exclusively on rural locations. HMA makes money by introducing efficient contracting systems and recruiting doctors, including specialists, to work in its hospitals. It also sets up physician practices, placing doctors in small towns like Bunn, N.C. (population 2,000), to feed patients into its hospital in Louisburg, about 20 miles away. "We don't put big HMA labels on the sign of our hospitals," he says. "We become part of the community."

That's important to the rural dwellers marketers are trying to reach. To Saleh Abraham, Canadian, Tex., is the place he grew up, the place his great-grandfather settled in after leaving Lebanon. It's the place he wants to raise his kids. A roomful of whirring computers three flights up at the top of Canadian's tall building lets him do that without sacrificing much in the way of professional opportunity. With a Lexus and a Chevy Suburban in the driveway and catalogs from Neiman Marcus, Bloomingdale's and Eddie Bauer on the coffee table, he hasn't sacrificed many material pleasures either. "The only things we focus on here are work and family. Nothing else gets in the way. No distractions. That's why I want to live here and one of the reasons why my business has done so well here," says Abraham. And with a freshly opened mail-order cheesecake on the table in front of him, life in Canadian is sweet.

*By David Greising in Quincy, Ill., with Kate Murphy in Canadian, Tex., and bureau reports*

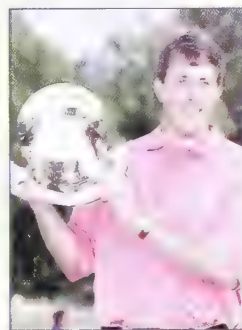
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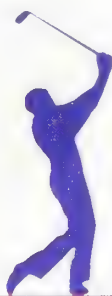
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# GOOD THINGS COME IN SMALL-CAP PACKAGES

Technology stocks made growth funds the stars of the third quarter

As quarterly earnings reports start streaming across the news wires, many analysts are holding their breath, fearful that Corporate America's powerful earnings engine will slow down. That doesn't worry managers of this quarter's top-performing mutual funds, however: Almost all are growth managers who benefited from a focus on technology stocks and other niche holdings that have the potential for years of above-average earnings growth—regardless of any economic slowdown.

Small-cap funds made one of the biggest comebacks in the third quarter, emerging with a 12.4% total return, vs. the Standard & Poor's 500-stock index's 7.2% return. While momentum is slow-

ing in the large-cap stock market indices, the small- and midcap indices are gaining strength. The tech-heavy NASDAQ Composite Index and the Standard & Poor's Smallcap 600 Index both are up more than 12% for the quarter, and even the Standard & Poor's Midcap 400 is up more than 9%.

But a broad range of equity fund investors enjoyed strong returns. A soaring stock market helped U.S. diversified equity funds rack up an average 9% return in the third quarter, including reinvestment of dividends and capital gains. Bond funds, meanwhile, barely budged. The average taxable bond fund eked out a 1.4% return; tax-free bond funds averaged a 1.7% gain.

Although small-cap funds are king of

the hill, the megafunds were no slouches in the third quarter. The \$13.1 billion aggressive-growth Twentieth Century Ultra Investors Fund won the top slot among the industry titans with its 17% return. In second place was \$13.3 billion Fidelity Contrafund, which gained 11% to outperform \$51.6 billion Fidelity Magellan Fund, which weighed in with a 10.8% total return. The three megafunds made big bets on tech stocks.

**EARTHQUAKE RECOVERY.** Pure technology funds maintained their ranking as the best-performing sector funds. The 21 technology funds tracked by Chicago-based Morningstar Inc. had an average total return of 17.4% in the third quarter. The fast-recovering health-care sector took second place, with 14.3%

## The Best Returns

|                                      | TOTAL RETURN* |                                       | TOTAL RETURN* |
|--------------------------------------|---------------|---------------------------------------|---------------|
| MERRILL LYNCH TECHNOLOGY B           | 27.3%         | SIT SMALL CAP GROWTH                  | 20.2%         |
| PBHG SELECT EQUITY                   | 26.1          | ALGER MIDCAP GROWTH                   | 20.1          |
| WASATCH MICRO-CAP                    | 25.9          | TWENTIETH CENTURY VISTA INV.          | 20.1          |
| ALGER CAPITAL APPRECIATION           | 24.9          | MFS EMERGING EQUITIES                 | 19.8          |
| KEYSTONE AMERICA HARTWELL EMERG GR A | 24.4          | USAA AGGRESSIVE GROWTH                | 19.8          |
| DOMINION INSIGHT GROWTH              | 24.2          | IVY EMERGING GROWTH A                 | 19.6          |
| GOVETT SMALLER COMPANIES A           | 22.7          | PERKINS OPPORTUNITY                   | 19.5          |
| REGIS RICE HALL JAMES SMALL CAP      | 22.7          | JOHN HANCOCK SPECIAL EQUITIES A       | 19.3          |
| PUTNAM OTC EMERGING GROWTH A         | 22.2          | TURNER SMALL CAP EQUITY               | 19.3          |
| FRANKLIN GLOBAL HEALTH CARE          | 21.7          | JOHN HANCOCK GLOBAL RX A              | 19.1          |
| BULL & BEAR SPECIAL EQUITIES         | 21.6          | WARBURG PINCUS JAPAN OTC COMM.        | 19.1          |
| ALGER SMALL CAPITALIZATION           | 21.4          | DEAN WITTER DEVELOPING GROWTH SECS.   | 19.0          |
| PIC SMALL CAP GROWTH                 | 21.4          | RSI RETIREMT. TRUST EMERG. GRTH.EQTY. | 19.0          |
| SHELBY                               | 21.3          | CAPPIELLO-RUSHMORE EMERGING GROWTH    | 19.0          |
| VAN ECK ASIA INFRASTRUCTURE A        | 21.2          | NAVELLIER AGGRESSIVE SMALL CAP EQUITY | 18.9          |
| PARKSTONE SMALL CAP INV. A           | 21.0          | PBHG GROWTH                           | 18.9          |
| FORTIS ADVANTAGE CAPITAL APPREC. A   | 20.8          | PIN OAK AGGRESSIVE STOCK              | 18.9          |
| IDEX II AGGRESSIVE GROWTH A          | 20.8          | TCW/DW SMALL CAPITALIZATION GROWTH    | 18.9          |
| ROBERTSON STEPHENS VALUE + GROWTH    | 20.7          | AMERICAN HERITAGE GROWTH              | 18.6          |
| FIDELITY SELECT COMPUTERS            | 20.6          | NEW USA MUTUAL                        | 18.6          |
| FIDELITY SELECT ELECTRONICS          | 20.6          | UNITED SCIENCE & TECHNOLOGY A         | 18.6          |
| SMITH BARNEY SPECIAL EQUITIES B      | 20.6          | CHESAPEAKE GROWTH                     | 18.5          |
| PACIFIC HORIZON AGGRESSIVE GROWTH    | 20.4          | T. ROWE PRICE SCIENCE & TECHNOLOGY    | 18.5          |
| PBHG LARGE CAP GROWTH                | 20.2          | BT INVESTMENT EQUITY APPRECIATION     | 18.4          |
| IAI EMERGING GROWTH                  | 20.2          | BT INVESTMENT CAPITAL APPRECIATION    | 18.4          |

Small-cap tech stocks boosted growth funds. Holdings of health-care stocks such as HMOs and medical-device makers paid off in spades, as did finance stocks.

\*APPRECIATION: 1 US  
REINVESTED DIVIDENDS AND  
CAPITAL GAINS: 1 - FORE TAXES.  
JULY 1-SEPT. 22, 1995  
DATA: MORNINGSTAR INC.

ds specializing in financial  
ks, such as those of banks and  
rers, also continued to be  
ng performers, up 11.2%.

tech stocks fueled many of the  
ty fund leaders to the top of  
pack. The quarter's top-per-  
ring fund, in fact, is the \$1.2  
on Merrill Lynch Technology  
d B, which chalked up a  
% return. The fund had a dis-  
ous first half, when the 42% of  
fund that was in Japanese  
nology stocks got clobbered  
r the Kobe earthquake. "We  
ously made a mistake," says  
manager James K. Renck.  
"I've tried to turn it around.  
re very happy about the way  
gs are going now."

Renck's nightmare came to an  
when he decided to take a  
on his Japanese holdings and  
e money into "a select group of  
stocks" that he hoped would beat  
ysts' earnings consensus. Renck's  
e is to take concentrated positions.  
top 12 holdings (which he doesn't  
t to disclose for now) make up 80%  
e fund.

ome tech investors, while still posi-  
on the sector, are hedging their  
James L. Callinan, senior portfolio  
ager of the \$1 billion Putnam OTC  
erging Growth A fund, saw it earn a  
% return as a result of having about

## How the Big Funds Fared

| FUND                            | TOTAL<br>RETURN* | ASSETS**<br>BILLIONS |
|---------------------------------|------------------|----------------------|
| FIDELITY MAGELLAN               | 10.8%            | \$51.6               |
| INVESTMENT COMPANY OF AMERICA   | 6.3              | 23.5                 |
| WASHINGTON MUTUAL INVESTORS     | 9.1              | 16.1                 |
| FIDELITY PURITAN                | 4.9              | 14.5                 |
| VANGUARD INDEX 500              | 7.4              | 14.1                 |
| VANGUARD/WINDSOR                | 8.1              | 13.4                 |
| FIDELITY CONTRAFUND             | 11.0             | 13.3                 |
| TWENTIETH CENT. ULTRA INVESTORS | 17.0             | 13.1                 |
| INCOME FUND OF AMERICA          | 5.4              | 12.5                 |
| FIDELITY GROWTH & INCOME        | 7.9              | 12.2                 |

\*APPRECIATION PLUS REINVESTED DIVIDENDS AND CAPITAL GAINS, BEFORE  
TAXES, JULY 1-SEPT. 22, 1995 \*\*AS OF SEPT. 22

DATA: MORNINGSTAR INC.

5% its holdings in America Online and  
modern maker U.S. Robotics Inc. at the  
start of the third quarter. Lately, he  
has been increasing his holdings in  
health-care stocks, hoping they'll offset  
any correction in tech stocks. His small-  
cap picks include EmCare Holdings Inc.,  
which provides physician services to  
emergency departments, and I-Stat  
Corp., which makes blood analyzers. A  
larger-cap favorite is Horizon Health-  
care Corp., a nursing home chain.

The second-best performing fund,

\$72.5 million PBHG Select Equity,  
racked up a 26.1% gain. The fund  
has not proved it can weather a  
down market, having only opened  
in April. But portfolio manager  
James D. McCall is a veteran  
growth manager who also man-  
ages the PBHG Large-Cap Growth  
Fund. McCall's challenge: sift  
through the top 10% of an 850-  
stock universe to find the 25 to 30  
stocks that will have the strong-  
est earnings growth. His largest  
holding is WorldCom, a U.S. long-  
distance phone company that he  
thinks will benefit from dereg-  
ulation and consolidation. Tech  
stocks such as Xilinx Inc. and LSI  
Logic Corp. are among his largest  
holdings, but McCall also has ex-  
posure to health care through  
managed-care company Oxford  
Health Plans Inc. and medical de-  
vice maker Boston Scientific Corp.

**RAH-RAH.** In third place is another new-  
comer, the \$25 million Wasatch Micro-  
Cap Fund, which is up 25.9% since it  
opened on June 19. It's a sister fund to  
the \$293.7 million Wasatch Aggressive  
Equity Fund, which closed to investors  
in mid-July. Robert Gardiner co-manag-  
es it with small-cap growth guru Samuel  
S. Stewart Jr., manager of the ag-  
gressive equity fund. Gardiner looks for  
companies with market capitalizations  
from \$10 million to \$200 million. He

## The Worst Returns

| TOTAL RETURN*                        |       | TOTAL RETURN*                         |       |
|--------------------------------------|-------|---------------------------------------|-------|
| EV MARATHON GREATER INDIA            | -7.4% | WRIGHT EQUIFUND-BELGIUM/LUXEMBOURG    | -0.2% |
| RYDEX URSA                           | -5.3  | ALLIANCE ALL-ASIA INVESTMENT B        | -0.1  |
| PIONEER INDIA A                      | -4.8  | SEI INTERNATIONAL EMERGING MARKETS A  | -0.1  |
| WRIGHT EQUIFUND-JAPAN                | -3.1  | PARNASSUS                             | 0.0   |
| BLANCHARD EMERG. MARKETS GRTH & INC  | -2.4  | EV MARATHON EMERGING MARKETS          | 0.1   |
| AETNA ASIAN GROWTH ADV               | -2.2  | NEW ENGLAND INTERNATIONAL EQUITY C    | 0.1   |
| ASIA HOUSE ASEAN GROWTH              | -2.0  | LOOMIS SAYLES INTERNATIONAL EQUITY    | 0.2   |
| MORGAN STANLEY ASIAN GROWTH A        | -1.5  | MERRILL LYNCH DRAGON B                | 0.2   |
| DREYFUS CAPITAL VALUE A (PREMIER)    | -1.3  | VAN ECK ASIA DYNASTY B                | 0.2   |
| FRANKLIN TEMPLETON JAPAN             | -1.3  | CENTURION T.A.A.                      | 0.3   |
| DFA CONTINENTAL SMALL COMPANY        | -1.1  | GOLDMAN SACHS ASIA GROWTH             | 0.4   |
| LINDNER BULWARK                      | -1.0  | AMT CAPITAL HLM INTERNATIONAL EQUITY  | 0.4   |
| STEADMAN INVESTMENT                  | -1.0  | COLONIAL NEWPORT TIGER Z              | 0.4   |
| NEW ENGLAND BALANCED C               | -0.9  | MATTHEWS ASIAN CONVERTIBLE SECURITIES | 0.4   |
| NEW ENGLAND VALUE Y                  | -0.8  | EVERGREEN INTERNATIONAL EQUITY B      | 0.5   |
| WRIGHT EQUIFUND-SWITZERLAND          | -0.8  | FIDELITY SOUTHEAST ASIA               | 0.5   |
| REMBRANDT ASIAN TIGERS INV           | -0.7  | DFA INTERNATIONAL SMALL CAP VALUE     | 0.6   |
| TCW GALILEO ASIA PACIFIC EQUITY      | -0.7  | EV TRADITIONAL GREATER CHINA GROWTH   | 0.6   |
| WRIGHT EQUIFUND-GERMANY              | -0.7  | GAM ASIAN CAPITAL                     | 0.7   |
| QUANTITATIVE FOREIGN FRONTIER ORD    | -0.6  | T. ROWE PRICE NEW ASIA                | 0.7   |
| QUANTITATIVE INTERNATIONAL EQTY ORD  | -0.6  | REGIS MJI INTERNATIONAL EQUITY        | 0.7   |
| JOSHUA MEDIA                         | -0.5  | SIT DEVELOPING MARKETS GROWTH         | 0.8   |
| LEXINGTON CROSBY SMALL CAP ASIA GRTH | -0.5  | SCUDDER GOLD                          | 0.8   |
| DFA EMERGING MARKETS                 | -0.4  | TCW GALILEO EMERGING MARKETS          | 0.9   |
| IVY CANADA A                         | -0.3  | VOYAGEUR INTERNATIONAL EQUITY A       | 1.0   |

\*APPRECIATION PLUS  
INVESTED DIVIDENDS AND  
CAPITAL GAINS BEFORE TAXES,  
JULY 1-SEPT. 22, 1995

DATA: MORNINGSTAR INC.

Investing  
assets  
abroad, say in  
India, China,  
or Japan,  
bruised  
portfolios.  
Asian growth  
funds actually  
shrank. Risky  
emerging-  
market funds  
also wound  
up in the red.



## Equity Funds To Financial Assets

\*APPRECIATION PLUS  
REINVESTED DIVIDENDS AND CAPITAL  
GAINS BEFORE TAXES, JULY 1-SEPT.  
22, 1995

DATA: MORNINGSTAR INC.

|                 | TOTAL RETURN* |                             | TOTAL RETURN* |
|-----------------|---------------|-----------------------------|---------------|
| TECHNOLOGY      | 17.4%         | UTILITIES                   | 5.4%          |
| HEALTH CARE     | 14.3          | BALANCED                    | 5.0           |
| SMALL COMPANY   | 12.4          | REAL ESTATE                 | 5.0           |
| MAXIMUM GROWTH  | 12.3          | ASSET ALLOCATION            | 4.6           |
| FINANCIAL       | 11.2          | EUROPE STOCK                | 4.6           |
| COMMUNICATION   | 10.5          | FOREIGN STOCK               | 4.6           |
| GROWTH          | 8.8           | NATURAL RESOURCES           | 3.9           |
| SPECIALTY-MISC. | 6.9           | DIVERSIFIED EMERGING MARKET | 3.0           |
| GROWTH & INCOME | 6.8           | PACIFIC STOCK               | 2.9           |
| EQUITY-INCOME   | 6.2           | U.S. DIVERSIFIED EQUITY     | 9.0           |
| WORLD STOCK     | 6.2           | ALL EQUITY FUNDS            | 7.8           |
| PRECIOUS METALS | 5.5           | S&P 500 INDEX               | 7.2           |

**Pure technology funds continued their rapid ascent. Health-care funds staged a comeback, bumping financial funds from the No. 2 slot they held in the second half.**

wants stocks that can hike earnings by more than 15% annually to "double, triple, become 10 times their size over the next three to five years." Gardiner likes \$60 million market-cap National Dentex Corp., the largest U.S. dental lab company, as well as Varsity Spirit Corp., which runs cheerleading camps and sells cheerleading uniforms. "These are small companies that aren't dependent on the economy but on executing their own business plan," he says.

While investing in the U.S. generally paid off, going overseas wasn't worth the trip. International equity funds returned on average just 4.6%. Funds investing in India have suffered from the country's volatile political situation, and investor confidence was badly shaken when a state government in India moved to cancel a power plant contract with Houston-based Enron Corp. Investors' jitters helped make EV Marathon Greater India the worst-performing fund in the third quarter, down 7.4%. A new fund category tracked by Morningstar, the diversified emerging-market group,

opened with the worst equity fund group performance for the quarter; its 54 funds averaging a return of 3%.

Investors also saw ho-hum returns in bond funds this quarter as the rally petered out. The best performers were funds that invest in convertible debt. Convertibles offer a steady income but also give the holder the option of converting the bond into a set number of shares in the issuer's stock. Interest rate decreases have made convertibles more attractive. Fund manager Andrew A. Davis steered the Retirement Planning Funds of America Convertible Securities Fund—recently renamed Davis Convertible Securities Fund—to an 8.4% total return by investing in financial and technology convertible securities.

High on the list of the best bond funds is a shocker: Loomis Sayles Global Bond Fund, with a 7.8% return. Most of its peers wound up on the worst-performing list of taxable bond funds, with the average return for international bond funds just 1.8%. But the Loomis Sayles fund benefited from having

hedged its positions back into the dollar before the greenback's recovery against the yen and the mark. The fund's focus on value directed it to smaller countries that it considers undervalued, such as Italy, Sweden, Ireland, and Canada. Fund manager John de Beer favors Ireland and Canada for their low inflation and strong debt-reduction programs.

Growing fears of a market peak did not seem to deter investors from pouring more money into equity funds in the third quarter. The inflow into stock funds in August was \$13.2 billion, a slight drop from July's \$13.9 billion cash flow. Bond and income funds also attracted investors, drawing in \$674.3 million in new cash flow in August—a big bump-up from July's \$41.9 million inflow and from June's \$3.3 billion outflow.

**WALLFLOWER'S LAMENT.** A closer look at week-by-week mutual-fund cash flows sheds light on just where that money is going. According to Robert Adler of AMG Data Services, inflows into technology funds have been dropping steadily and even turned negative in three of the last four weeks. Flows into aggressive growth and small-cap growth funds, however, remain strong. Some money is being squirreled away in money-market funds, which increased assets from \$717 billion to \$749 billion, mainly from new inflows. And taxable bond funds—particularly high-yield, investment-grade and high-quality funds—have seen renewed interest from investors.

Overall, investors keep pouring money into mutual funds, and for good reason: To stay on the sidelines was to miss out on sizzling returns. Investors may feel jittery moving into the fourth quarter, fearing that the stock market may cool off a bit. But the evidence from the past quarter is that the average mutual fund can outperform the stock market. And some fund managers can leave the Dow in the dust.

*By Suzanne Woolley in New York*

### TAXABLE FUNDS

### TAX-FREE FUNDS

|                                     | TOTAL RETURN* |                                      | TOTAL RETURN* |
|-------------------------------------|---------------|--------------------------------------|---------------|
| NICHOLAS-APPLEGATE INC & GROWTH C   | 8.6%          | MAS PA MUNICIPAL                     | 4.1%          |
| RETIREMENT PLANNING CONVERT SECS A  | 8.4           | ACHIEVEMENT ID MUNICIPAL BOND RET A  | 3.8           |
| LEXINGTON CONVERTIBLE SECURITIES    | 7.9           | MAS MUNICIPAL                        | 3.7           |
| BOND FUND FOR GROWTH A              | 7.7           | FRANKLIN CA INTERM-TERM TAX-FR INC   | 3.3           |
| LOOMIS SAYLES GLOBAL BOND           | 7.7           | STEPSTONE CA TAX-FREE BOND INVSTMT   | 3.1           |
| MERRILL LYNCH AMERICAS INCOME B     | 7.7           | VOYAGEUR AZ TAX-FREE A               | 3.1           |
| SBSF CONVERTIBLE SECURITIES         | 7.1           | FRANKLIN FEDERAL INTERM-TERM T/F INC | 2.9           |
| FRANKLIN CONVERTIBLE SECURITIES     | 6.8           | NEW YORK MUNI                        | 2.9           |
| WADDELL & REED INTERNATIONAL GROWTH | 6.7           | SOUTH DAKOTA TAX-FREE                | 2.9           |
| CALAMOS CONVERTIBLE                 | 6.4           | VOYAGEUR FL LIMITED-TERM TAX-FREE A  | 2.9           |
| AVERAGE OF 1549 FUNDS               | 1.41          | AVERAGE OF 1550 FUNDS                | 1.67          |

\*APPRECIATION PLUS REINVESTED DIVIDENDS AND CAPITAL GAINS BEFORE TAXES, JULY 1-SEPT. 22, 1995

DATA: MORNINGSTAR INC.

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## REAL ESTATE

# NO REST FOR THESE WEARY INVESTORS

They won't see cash yet as Atlantic Gulf rolls the dice again

**M**any of the beleaguered customers of General Development Corp., the huge Florida developer, may feel mired in an Everglades backwater. During the 1980s, lured by the company's pitches, investors eagerly bought up GDC houses as well as lots in its huge developments. While GDC didn't mimic the swampland sales of the worst of the state's developers, its high-pressure and misleading sales practices led to fraud indictments against the company and four top officers in 1990. After the executives were convicted and served about two years of their sentence, an appeals court last March ordered them released on bail while it reviews the case. Also in 1990, GDC filed for bankruptcy and pleaded guilty to one count of mail fraud. It emerged from bankruptcy in 1992 with new management and a new name, Atlantic Gulf Communities Corp. Its goal: to liquidate its assets, mainly raw land in 15 Florida counties, and make restitution to GDC customers.

But the story has been taking a curious turn. J. Larry Rutherford, 49, a well-regarded developer who became



**RUTHERFORD:** Keying in on Florida's boomtowns

chief executive in 1991, is turning out to be more ambitious than most people thought. He wants to transform AGC into a major player. Says a company director: "Larry is interested in the grand designs, the great ventures, and not in presiding over a liquidation." Rutherford is plowing millions into developing homesites in the state's fastest-growing communities. "We're so close to turning this thing around," he says.

But GDC's customers, who received shares and unsecured notes in AGC as part of the bankruptcy and fraud settlement and may have expected a quick payout, shouldn't get their hopes up. AGC it turns out, has its own passel of problems. If Rutherford doesn't deliver, customers could find themselves back

in the big swamp. Retiree Muriel Buckley and her husband, John, received the bonds totaling \$2,100 after the bankruptcy court in the GDC case found they had been defrauded of \$20,300—an amount above market value of a Silver Springs Shores home that they had bought. "They're unsecured," she says of the bonds. "If something happens, we get nothing."

In December, 1996, the Buckleys and about 20,000 other GDC customers are supposed to start receiving part of \$30 million in debt repayment. That's a lot of money—especially from a company that made only \$1 million last year in sales of \$106 million. Robertson, Stephens & Co. analyst Jay P. Leupp estimates that AGC's revenues will jump to \$142 million this year, but figures are lost at \$3.1 million.

**CHINA EXIT?** Atlantic Gulf's other headache is the 65,000 acres of land on its balance sheet, which cost the company more than \$20 million a year. "It's the anchor around the company's neck," says Larry Seidman, who owns more than 20,000 shares. He isn't the only impatient shareholder. In July, Chemical Bank, then the company's biggest investor, unloaded its 800,000-share position. That pummeled AGC's already slumping stock, which is down almost 50% from its 52-week high.

Rutherford has been criticized by some AGC shareholders and board members for pursuing ill-fated projects instead of realizing the value in the company's land holdings. One example: Rutherford's failed foray into China. Since 1993, the company has spent more than \$5 million on a 4,000-acre project near the city of Nanjing. Rutherford believed he had scored a coup in the venture, which sought to turn farmland into a mixed-use urban center. But three years later, no progress has been made, and AGC is looking for an exit. Rutherford argues that AGC has met unexpected obstacles. Much of the land it inherited from GDC, for instance, is in

## THE ATLANTIC GULF SAGA:

Will Homeowners Be Burned Twice?

**MARCH, 1990** General Development Corp., a subsidiary, and four top executives are indicted on charges of fraud. GDC files for bank-

ruptcy in April. In November, the company pleads guilty to one count of mail fraud and agrees to pay restitution to customers.

**MARCH 1991** Larry Rutherford, a Florida developer, named CEO.

**MARCH, 1992** GDC emerges from bankruptcy under the name Atlantic Gulf. Plans to

sell land and other assets to make good on restitution plan to customers, who are given bonds and stock.

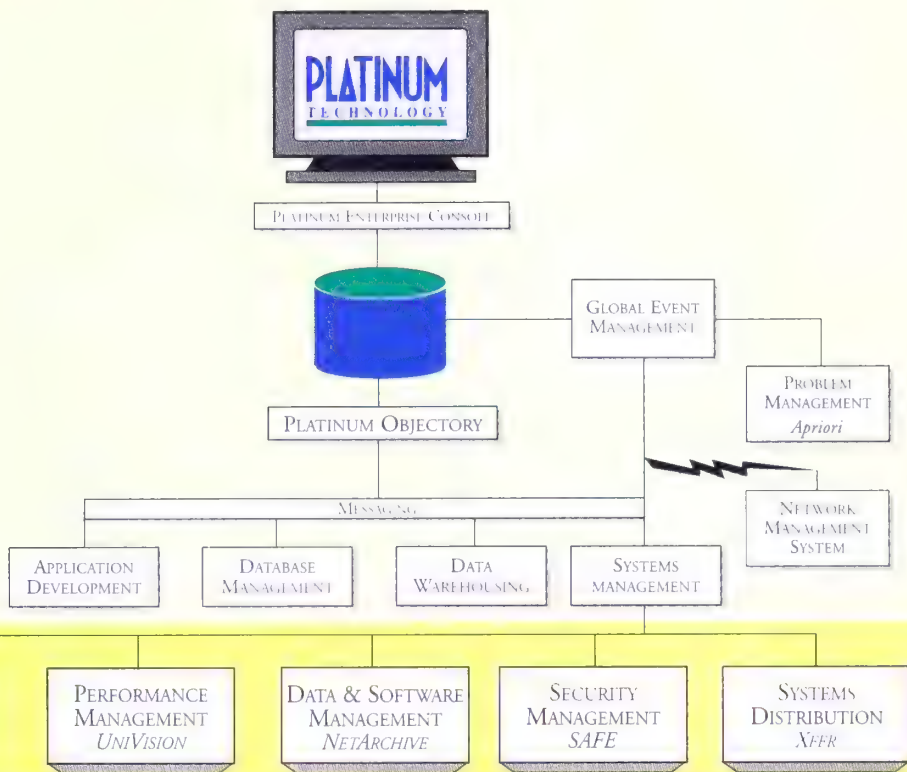
**1993-1994** The company starts acquiring land to pursue development projects. Rutherford comes under criticism from shareholders for trying to build a real estate empire instead of liquidating existing land holdings.

**AUGUST, 1995** The company speeds up land sales and, to cut costs, eliminates 90 jobs, or 40% of its workforce. Yet it faces a future cash crunch. In December, 1996, the company, which is losing money, must begin making \$200 million in debt repayments to homeowners.

DATA BUSINESS WEEK

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Florida's backcountry, where demand for developers and builders is low. Attempts to rezone the parcels for agricultural use, which would have made the land more attractive, were opposed by local municipalities for fear of losing a potentially lucrative tax base. Atlantic Gulf has also been trying to reacquire two utilities developed by GDC, which are in communities where many of the cheated customers reside. When the two communities used eminent domain to seize the utilities, AGC filed suit to get a fair price. The company settled with one community and is still battling

the other. Rutherford did please shareholders in August by hiring a manager to sell land full-time and by vowing to cut 90 jobs by yearend. He also has been renegotiating with Bankers Trust New York Corp. on stretching the payback period for the \$200 million in notes that come due starting in December, 1996. But interest rates could be as high as 15%, Rutherford admits.

**AMBUSH PLAN.** Rutherford claims disputes within the AGC boardroom are more questions "of tactics and not strategy." The strategy now hinges, in part, on spending some \$15 million creating

homesites on land in the paths of Florida's fastest-growing suburbs, such as Tampa's. Some of the completed homesites already are being sold to builders.

Builders and real estate experts say the strategy is workable if AGC's cash commitment is minimal. "Their basic assumption is correct," says consultant Lewis Goodkin, "as long as they have the right land." But for Atlantic Gulf's long-suffering shareholders and bondholders who were once GDC customers, this is one they've heard before.

*By Antonio Fins with Gail DeGeorge in Miami*

## STOCKS

# AN END RUN AROUND WALL STREET

Many companies are selling stock directly to small-fry investors

Dean Witter Reynolds Inc., the brokerage firm, will book some \$900 million in commissions this year for buying and selling securities for customers. But if you want to buy stock in Dean Witter itself, you don't need to pay a commission to a broker. The firm's parent recently became one of a growing number of companies to institute direct-purchase stock plans, making it easy for investors to become shareholders without punching Wall Street's meal ticket.

The purpose of "no-load" stock plans—so called because of their similarity to no-load mutual funds that investors buy directly from a fund company—to woo individual investors. Some 8,500 of Barnett Banks' 44,000 registered shareholders came on board by way of the 18-month-old direct-investment plan. "It's helping us maintain our retail base of shareholders," says Catherine Cosby, the corporate secretary.

**MOM AND POP.** Why the loss? In recent years, many folks have opted for mutual funds rather than individual stocks. And individual investors, who reasonably don't take possession of their certificates, tend to remain anonymous, and companies would like to know who they are. "You can get lists from brokers, but they're usually so old and stale they're worthless," says Gor-

don G. Garney, a shareholder-relations executive at Mobil Corp.

Many companies have lost individual investors by showing them the door, running "odd-lot" buyback programs to encourage shareholders with fewer than 100 shares to leave the fold. The thinking was that these small shareholders cost too much to service. Now, many corporations realize the value in hav-

Charles B. Carlson, who follows no-load stocks in his newsletter *DRIP Investor*, says consumer-oriented companies are realizing shareholders are customers, too. George M. Holston, an investor-relations manager at Texaco Inc., says 76% of shareholders surveyed said they buy or are inclined to buy Texaco products. Most companies with direct-investment plans are ones that market their products and services to consumers.

In direct-investment plans, almost no investor is too small. Exxon, Mobil, and Texaco, for instance, ask for a \$250 initial investment. Although that will buy just a few shares, the hope is that these investors will build their stakes over time. Regions Financial Corp., an Alabama banking company, has a \$20 initial investment, which at the current price buys only about a half a share of stock.

Companies can afford to sell stock in such small amounts because these programs are linked into an existing dividend reinvestment plan, known as a DRIP. Such plans allow shareholders to reinvest dividends in more shares—in small amounts and fractional shares.

Most of the time, investors' purchases are fulfilled through open-market orders. But some companies issue new equity, too. NorAm Energy Corp., a Houston-based gas utility, launched its plan 10 months ago to help repair its balance sheet and has sold about 1 million of the 5 million shares authorized, raising around \$6 million.

While the no-load stock concept is gaining ground, there are still only 74 companies with such programs. But Carlson expects that as many as 500 companies will offer direct investments within the next five years. "Big, well-known companies are going into this," he says, "and that gives it credibility."

*By Jeffrey M. Laderman in New York, with Gary McWilliams in Houston*

## Bypassing Brokers

Over the last year, these companies have adopted plans that allow investors to purchase stock directly.

|                             |                              |
|-----------------------------|------------------------------|
| <b>ATMOS ENERGY</b>         | <b>NORAM ENERGY</b>          |
| <b>BOB EVANS FARMS</b>      | <b>PINNACLE WEST CAPITAL</b> |
| <b>CAPSTEAD MORTGAGE</b>    | <b>PORTLAND GENERAL</b>      |
| <b>DEAN WITTER DISCOVER</b> | <b>PROCTER &amp; GAMBLE</b>  |
| <b>HOUSTON INDUSTRIES</b>   | <b>TENNECO</b>               |
| <b>MONTANA POWER</b>        | <b>UTILICORP UNITED</b>      |
| <b>MORTON INTERNATIONAL</b> | <b>WISCONSIN ENERGY</b>      |

DATA: DRIP INVESTOR

ing Mom and Pop on board. "Surveys show individuals really do hold long-term," says Louis M. Thompson Jr., president of the National Investor Relations Institute. "Only about 1% of them are active traders." Compare that to mutual-fund managers, who turn over 75% of their portfolios every year. And individuals are more likely to vote their shares with management.

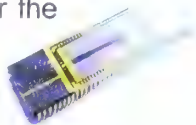
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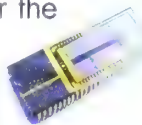




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BY GENE G. MARCIAL

## THE WACHOVIA AND SUNTRUST TANGO

All year, the stock of bank holding company Wachovia (WB) has seen-sawed between 34 and 36—until early August, when heavy buying broke out. By mid-September, the shares hit 45. What's behind it all? Takeover talk.

"Wachovia has been in informal discussions with the people at SunTrust Banks (STI) for a possible merger," says one New York investment banker. There is so much to be gained on both sides that "it's almost irresponsible for them not to talk merger," he explains. What seems to be holding up a deal, he adds, is the unresolved question of who is going to run the merged companies. SunTrust declined comment although Chairman Jimmy Williams has said publicly he wasn't in a hurry to do a merger. Wachovia didn't respond.

Currently trading at 43, Wachovia is worth 55 to 60 in a buyout, figures one buyout pro. It operates 491 branches and has assets of \$43 billion. SunTrust, now at 66, has assets of \$44 billion and operates 650 branches. In a merger, the stock is worth at least 85, he estimates.

Analyst George Salem of Gerard Klauer Mattison gives a high percent-

20% higher with a merger.

A combined Wachovia-SunTrust would become the 10th-largest banking company, says Salem. The new combo would rival current banking mainstays in the Southern states, mainly Nations-Bank, First Union, and Barnett.

Wachovia has been regarded as one of the best in the industry in terms of management and financial performance. SunTrust, which was founded in 1985 when Trust Co. of Georgia and Sun Banks merged, is also no slouch. "Its 1994 return on equity of 18.5% and return on assets of 1.36% are hardly shabby," notes Salem.

Wachovia CEO L. M. (Bud) Baker Jr. will probably be CEO of the merged company, while SunTrust CEO Williams is likely to be the chairman, Salem believes. "These are sticky points," he says, but they will be overcome "simply because the stakes are too high."

## JUNIOR TAKEOVER TERRORS

Lawrence Seidman and Richard Whitman aren't exactly the "takeover terrors" that Icahn, Kravis, or LeBow are reputed to be. But they have made some buyout hits of their own. Because of their large stake in Crestmont Financial, they took control and later sold the company to New Jersey's Summit Bancorp. They also participated when Summit went into the arms of UJB Financial, a New Jersey bank holding company that agreed on Sept. 11 to buy Summit for \$1.2 billion in stock.

So what are Seidman, who heads Seidman & Associates, and Whitman, managing partner at Benchmark, buying now? IBS Financial (IBSF), a New Jersey savings-and-loan company, in which they have just acquired a 5% stake valued at \$7.2 million. Almost immediately the duo announced they would press management into taking steps "to realize the inherent value of IBS's franchise in a manner designed to maximize shareholder value." Assets total \$665 million, and the company operates of-

## HIGH STAKES FOR A RISING STAR



fices in Burlington, Camden, and Gloucester counties in New Jersey.

Management is rumored to have met with Seidman and Whitman to discuss proposals to boost the stock price, says investment manager Jim Awad, who has been accumulating shares in anticipation of a takeover. "There's no doubt that the stock is undervalued based on its assets and excess capital," says Awad. He values IBS shares, now at 16, at 20 to 25 in a takeover deal.

In the meantime, management has acknowledged that its stock is undervalued and decided to buy back as much as 5% of its own shares. That won't be enough, says Awad. He thinks Seidman and Whitman will press management to either use its excess capital to boost the stock or sell the company.

## LOCKING IN A WINNER?

Corrections Corp. of America (CXO) is one company with a real captive market: It's in the prison business. "It's the stock to own for at least the next 10 years if you're looking for a company that's dominant in an erupting market," says investment pro Andrew Lanyi of Ladenburg Thalmann.

Among Lanyi's biggest winners this year is Steris, up 168%, Alternati Resources, 127%, and PhyCor, 105%. Corrections, his most recent pick, has already jumped to 45 from 28 in early March. Lanyi insists the stock has a lot more upside room.

Why? Earnings are up. In 1994, they rose 51%, to 53¢ a share, on revenues of \$120 million. This year, earnings will zoom to 75¢ on revenues of \$185 million and then soar to \$1.31 a share next year on sales of \$275 million.

The privatization of prisons is the rise, says Lanyi, explaining Corrections' tremendous gains. The company is the leader in designing, building, and managing prisons and correctional facilities. The number of prison beds under contract with Corrections has grown from 9,331 at the start of 1994 to 21,675 by mid-1995.

"The business is not only recession-proof but counter-cyclical as well," notes Lanyi. It makes money when the economy is humming—and more money in bum times when crime speeds up and jails get more swollen with inmates. Corrections manages more than 40% of the privately run prison market, he notes. And that market is growing.

## UPWARD MOBILITY



age to the likelihood that Wachovia and SunTrust will do a "merger of equals" over the next few months. He bases this on their compatibility and the shareholder values that will be created by a deal.

He figures a merger would result in cost savings of \$310 million, or 25% of Wachovia's 1997 estimated expense base. The deal would immediately create a substantial earnings boost, Salem adds. Earnings in 1997 would be about



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# THIS PLANE ISN'T TAKING OFF

McDonnell Douglas' new jet could ground its commercial unit

One year ago, Harry C. Stonecipher swept into the corner office of McDonnell Douglas Corp. What a change. Brash, decisive, and a passionate salesman, the 59-year-old chief executive seemed everything his genteel, brainy, and often ponderous predecessor, John F. McDonnell, wasn't. Stonecipher, the first nonfamily member to run the aerospace company in its 75-year history, quickly made his mark internally: He gives shop-floor pep talks, pens personalized newspaper ads, and started casual Fridays at the company's stodgy St. Louis headquarters.

Stonecipher, however, seems to be stumbling where it really counts: turning around McDonnell's beleaguered commercial airline division, Douglas Aircraft Co. Last spring, Scandinavian Airlines

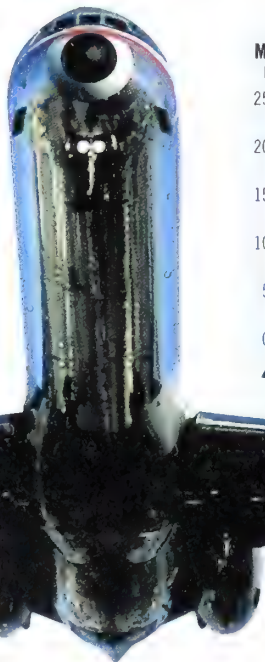
day (chart). Since 1991, operating earnings at the unit have plummeted from \$283 million to \$47 million.

Commercial aircraft, moreover, contributed just one-third of McDonnell's \$13.1 billion in 1994 revenue, dwarfed by sales of space and military equipment to the Pentagon, foreign military customers, and NASA. "If McDonnell Douglas hadn't had a profitable core of military

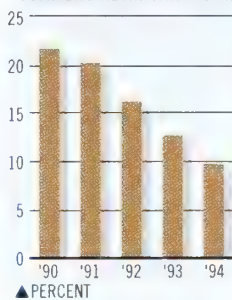
## SALT ON ITS TAIL



CEO HARRY STONECIPHER



McDONNELL DOUGLAS' SHARE OF COMMERCIAL AIRCRAFT SALES



DATA: NATWEST SECURITIES CORP

System scuttled a major order for McDonnell's proposed MD-95, instead inking a deal with Boeing Co. for 100-seat 737-600 jets. Then, on Sept. 19, news broke that negotiations for a major order of MD-95s with ValuJet were crumbling and that the Atlanta-based airline was warming instead to a bid from Airbus Industrie. The same day, McDonnell Douglas was compelled to issue a statement denying reports that its inability to secure orders for the MD-95 would force it to take on the Chinese government as an equity partner.

**EARNINGS PLUNGE.** Such woes have triggered new speculation that McDonnell may be forced to shut down its commercial jet business. In dozens of newspaper advertisements, Stonecipher has denied any plans to do so. But the company's 22% share of the commercial market five years ago has dwindled to just 9.8% to-

sales, the company would have gone bankrupt a long time ago," says Wolfgang Demisch, an aerospace analyst with BT Securities Corp.

Stonecipher, who was unavailable for comment, has seen battle before. After heading General Electric Co.'s jet-engine business, he spent seven years turning around Sundstrand Corp., a maker of aerospace and industrial products that had been mired in a military contract-fraud mess. An enthusiastic hands-on manager, he's well known for taking over troubled projects personally—as he has with McDonnell's new C-17 military transport plane.

What Stonecipher has in his favor at

McDonnell is a robust military business which generates nearly \$800 million in cash each year. That's more than enough to finance the launch of the MD-95. Industry observers say the company's decade-long commercial slide against rivals as Boeing and Airbus, coupled with its inability to secure orders for the MD-95, signal that it could eventually be forced out of the market. "The MD-95 is the last program that could help stay viable in the eyes of customers," says Nicholas Heymann, aerospace analyst with NatWest Securities Corp.

**MAINTENANCE WOES.** The launch of the MD-95, which will cost \$22 million to \$25 million apiece, is crucial. Its basic design is modeled largely on McDonnell's venerable DC-9, but it boasts a new engine and spruced-up nose and landing gear. That makes it an attractive complement to the reliable but gas-guzzling MD-80 jet.

Worldwide demand for MD-95-size planes is expected to exceed 800 by 2010, according to analysts. McDonnell is competing with new products from Boeing, Airbus, Daimler-Benz Aerospace's Fokker subsidiary, and Embraer's Avro. Says Robert J. Lanese, deputy president of McDonnell's Aerospace unit: "This is like the Olympic tri-

Without strong signs that McDonnell Douglas is a long-term player in the market, it's likely that many MD-95 orders will not materialize. Customers justly will worry about plane maintenance, upgrades, and competing leasing values. Over the past years, indeed, the market value of McDonnell Douglas' large, three-engine MD-11 has dropped 40%, analyst Heymann says, as rival aircraft makers have launched better-performing products.

For that reason, some analysts speculate, Stonecipher acknowledges the pressure for McDonnell Douglas to abandon its commercial business. But he also realizes that throwing in the towel completely could all but eliminate the current value of existing planes. The way the business is sinking, though, Stonecipher may have little left to lose.

By Ron Stodghill II in St. Louis, Mo.



**Edwin L. Artzt**  
Chairman, Executive  
Committee of the Board  
The Procter & Gamble  
Company



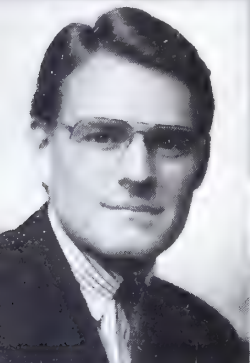
# NIGHTLY BUSINESS REPORT



**Charlotte Beers**  
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Ogilvy & Mather  
Worldwide

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Incorporated

## TAKING CHARGE: THE NEW AMERICAN LEADERSHIP



**Alfred M. Zeien**  
Chairman & CEO  
The Gillette Company

## Making \$ense Of It All.

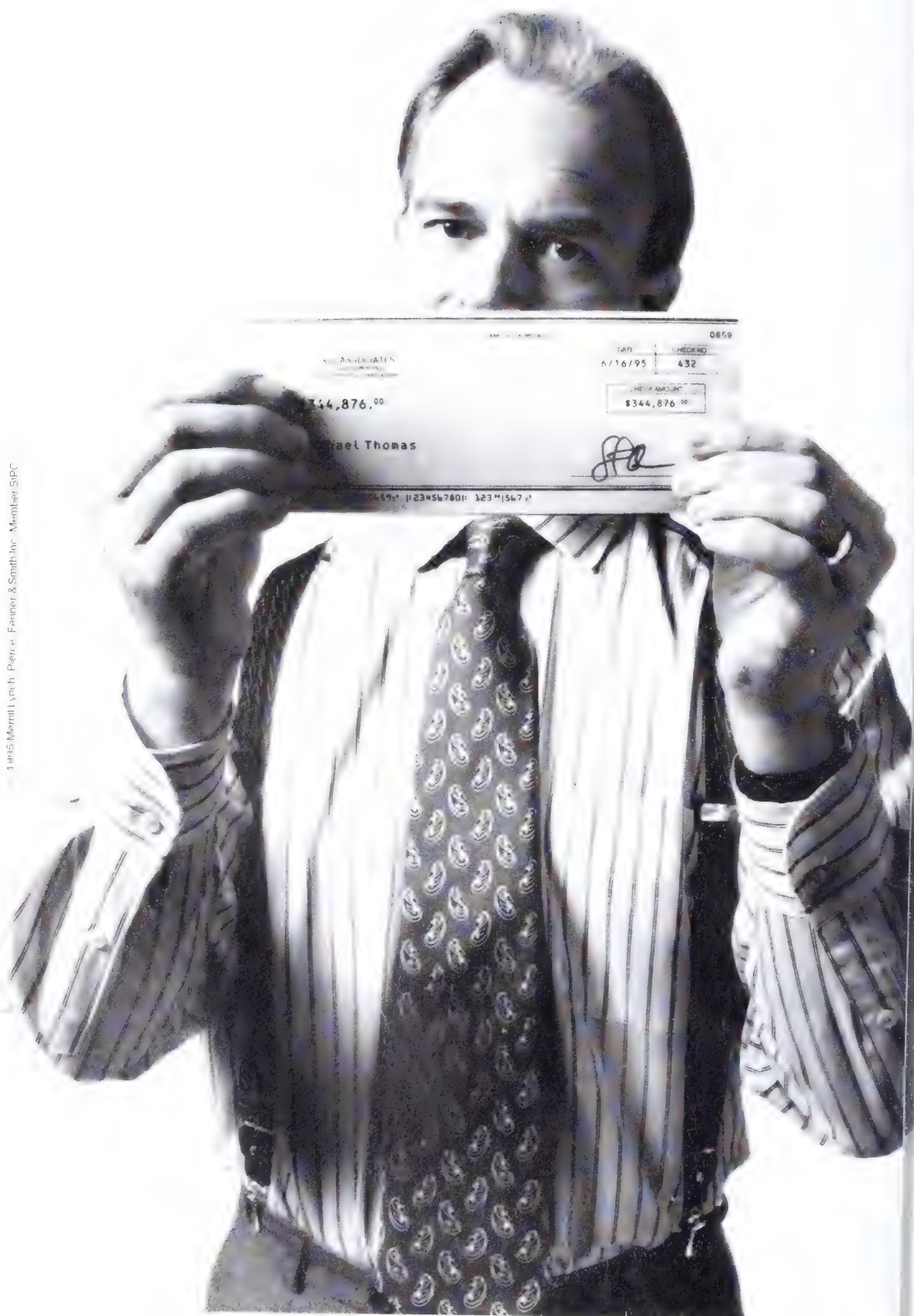
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## Cover Story

# RIDING HIGH

Corporate America now has an edge over its global rivals

Compaq's 1992 restructuring was one of those events that, with hindsight, marked a turning point. After years of losing sales to low-cost rivals, the personal computer maker struck back by sharply hiking productivity and cutting prices. By 1994, revenues had more than doubled, earnings had quadrupled, and Compaq Computer Corp. had leapt to the No. 1 position in the PC business, with a 13% market share. Now, in a quest for even faster growth, Compaq is investing in new information system overhauling manufacturing techniques, and chasing overseas sales. "For us to keep growing, we have to put in the state-of-the-art technology, make constant progress, and make constant improvements," says Compaq Chief Executive Officer David H. Hoffman. "If you stand still, you will fall behind."

It's a catchphrase for our era, the Age of Productivity. A sense of urgency is evident all around. Managements are reengineering operations and building an information infrastructure of computers, software, and telecom equipment. Giant AT&T splits itself into three separate companies to become a nimbler, more flexible competitor. Ford Motor Co. nearly pushed into the scrap heap by the Japanese juggernaut in the early 1980s, now runs some of the car industry's most productive plants. The U.S. semiconductor industry, with a bold bid for global market share, is constructing \$9 billion worth of new plant capacity in the U.S. Says Paul A. Allen, chief executive of Xerox Corp.: "I think inside corporate America everybody is more focused on being competitive and efficient than they ever have been."

All this ferocious activity is part of a comeback that restores U.S. dominance on reincarnation. For much of the past two decades, U.S. companies appeared to be no longer competitive with their foreign rivals. Many feared that America would follow the imperial powers such as Austria-Hungary and Britain into economic decline. Japan was poised to become the world's hegemonic economy, eclipsing the U.S.

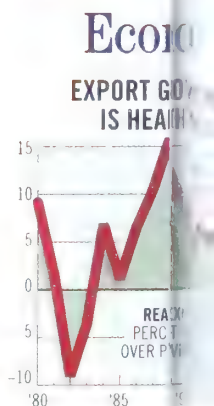
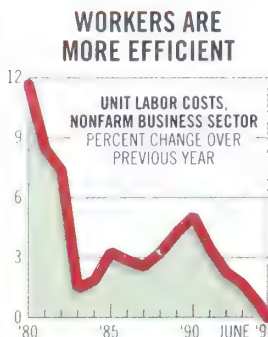
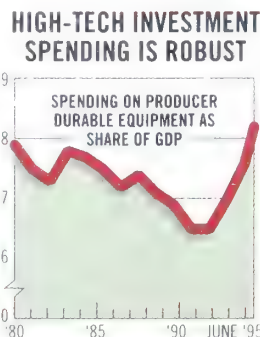
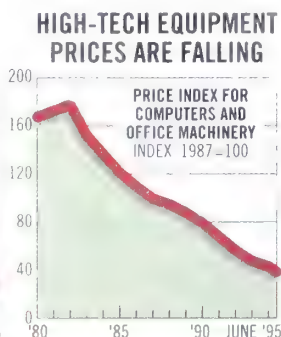
## The Productivity Bonanza

*The U.S. economy's edge should translate into prosperity*

**NONFARM BUSINESS PRODUCTIVITY**  
MEASURED BETWEEN BUSINESS CYCLE PEAKS  
DATA: BUREAU OF LABOR STATISTICS



## Driving Forces



DATA: COMMERCE DEPT., BUREAU OF LABOR STATISTICS; BLOOMBERG FINANCIAL MARKETS; BUREAU OF ECONOMIC ANALYSIS; CHALLENGER, GRAY & CHRISTMAS INC., BUSINESS WEEK

everything from autos to televisions. In 1986, when author John H. Fallows shared a beer with an English friend in Tokyo, the friend said: "Why don't you just face the fact that you're under-performers like us?" By 1988, Japan's stock market accounted for 44% of world-market capitalization, up from 17% in 1980, according to Morgan Stanley Capital International. In the same period, the U.S. stock market fell from 50% of the world market to 29%.

Today, Corporate America has embarked on a capital-spending boom. Corporate profits as a percentage of national income are far higher than they were in the 1980s. Unit labor costs have been flat over the past year, compared with an average annual increase of 4.1% in the 1980s, a clear sign of improved efficiency. The U.S. has also regained its primacy as the world's leading stock market, rising by 75% since 1990, while the Japanese market has plummeted by 50%.

Underlying these gains is a powerful upsurge in productivity. In the 1990s, nonfarm productivity has been rising

at a 2.2% rate, more than twice the anemic pace of the previous two decades. And in the fifth year of an economic expansion, a time when output per worker typically subsides, productivity posted a remarkable 3.5% year-over-year gain in the second quarter of 1995. "In a truly competitive global economy, U.S. performance has been outstanding," says Grady E. Means, head of strategy consulting services at Coopers & Lybrand. Adds William Lewis, director of the McKinsey Global Institute: "The U.S. has the highest productivity and the best job creation performance among the industrial countries."

**FRONTIER DAYS.** Small differences in productivity add up to big changes in income over time. If the U.S. raises its productivity trend growth rate by just 0.5% a year, to 1.5%, that increment cumulates to about \$300 billion over 10 years—sufficient to compensate for about three garden variety recessions, says Stephen S. Roach, economist at Morgan Stanley. If the current 2% pace remains, national output will rise about 10% more than it otherwise would over the next decade. Put somewhat differently, real per-capita gross domestic product in the U.S. increased by 1.75% a year from 1870 to 1990 to the world's highest level—from \$2,224 to \$18,258 (in 1985 dollars). Had the U.S. growth rate been just one percentage point less—0.75% a year—then real per-capita GDP in 1990 would have been \$5,519, or around Mexico's level and about \$1,000 less than Portugal's, according to calculations by Robert J. Barro, economist at Harvard University.

To be sure, the full extent of the productivity gains are



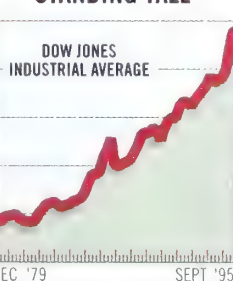
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## Downsides—For Now

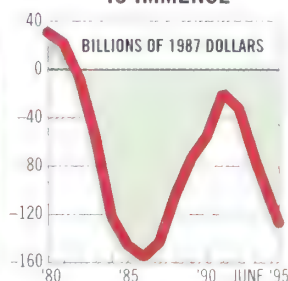
### RATE PROFITS SWELLING



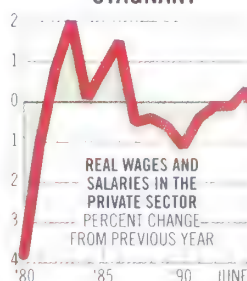
### THE MARKET IS STANDING TALL



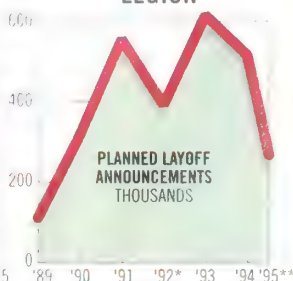
### THE TRADE DEFICIT IS IMMENSE



### WAGES ARE STAGNANT



### LAYOFFS ARE LEGION





muddled by some problems with the underlying statistics. The government's current 2.2% productivity number for the 1990s will be revised. Soon, government number-crunchers will introduce a new method for calculating economic growth that is likely to cut productivity growth by perhaps half a percentage point, estimates Edward McKelvey, senior economist at Goldman, Sachs & Co.

At the same time, most economists agree that the government numbers miss many of the biggest gains from higher productivity. The advantages to consumers from automated teller machines, affordable fax machines, and increased choice

of mutual funds do not show up in the figures. Moreover, by understating the ex-

tensive use of software, telecom gear, and other high-tech investment, the official statistics underestimate GDP and, by inference, productivity. For example, the current capital-spending upturn is centered on information technologies, but software expenditures are not counted as investment (except for software sold with computer hardware as a package). The addition of corporate software purchases could boost information-processing investment by more than 20%, according to the Bank Credit Analyst, an investment and business forecasting firm.

## Cover Story

The economy's productivity expansion follows a long tradition, which is hardly surprising. Whenever a major new technology such as computers is introduced into an economy or workplace, productivity falters as workers and managers struggle to master unfamiliar skills. Learning how to exploit frontier technology takes years of experimentation and organizational reshuffling. Over time, though, both management and labor move up the "experience curve." At the same time, additional innovations make technology easier to use, and falling prices speed the diffusion of the new technology. The payoff: higher productivity. Says Richard S. Belous, senior economist for the National Planning Assn.: "I would not be surprised if we see productivity growth that rivals the agricultural revolution and the manufacturing revolution."

**MAJOR PLAYERS.** The signs of resurgence are striking, especially from an international perspective. American companies are way ahead of almost all others in leading-edge hi-tech industries, from software to biotech to online services. The U.S. has 63 personal computers per 100 employed workers (including PCs at school and home) to Japan's 17, according to International Data Corp. The U.S. is the lowest producer among industrial nations, with unit labor costs rising more slowly than in either Japan or Germany. American manufacturers are 10% to 20% more productive than German or Japanese manufacturers, and the U.S. service sector

## WHY THE PRODUCTIVITY TIDE WILL LIFT ALL BOATS

**T**he U.S. economy is more productive and competitive than it has been in three decades. But the good news just doesn't wash with a lot of people.

Little wonder. Over the past two decades, real wages have been virtually flat, and the productivity-led recovery of the 1990s hasn't improved the situation. And in a nation where equality has always been a central idea, income inequality is rising. Dozens of books by liberals and conservatives alike, from Jeremy Rifkin's *The End of Work* to Sir James M. Goldsmith's *The Trap*, are stoking end-of-an-era pessimism in ways that echo the 1848 *Communist Manifesto* of Karl Marx and Friedrich Engels: "The modern labourer... instead of rising with the progress of industry, sinks deeper and deeper below the conditions of existence of his own class. He becomes a pauper, and pauperism develops more rapidly than population and wealth."

**REAL WEALTH.** But just as Marx far underestimated the eventual payoffs from the Industrial Revolution, so, too, are today's pessimists missing the coming gains from the Information Revolution. America's economic glass should be seen as half-full rather than half-empty.

For one thing, workers may be doing better than the recent wage data suggest. Real wages have declined by 0.2% annually over the past five years. But a congressionally appointed panel of econ-

omists, headed up by Michael Boskin, former head of the Council of Economic Advisers, argues that the consumer price index has been overstating inflation by at least a percentage point. If that's the case, then real wage gains are 0.8% a year. And hourly compensation—which includes retirement and medical benefits—would be up about 1.3%.

Many workers are also sharing in the boom in stocks and bonds for the first time ever, thanks largely to tax-deferred retirement savings plans such as 401(k)s and individual retirement accounts. Over the past five years, the value of equities and mutual funds held by households has jumped by \$2.4 trillion, to \$4.5 trillion, according to Joseph Carson, chief economist at Dean Witter Reynolds Inc. And it's the workers

who will reap the market gains in their retirement savings, not the companies as in traditional pension plans.

Workers are also bound to enjoy fatter paychecks follow higher productivity. Over long periods of time, productivity and wages track each other closely.



**OLD WAVE:** Typewriters helped revolutionize work—and boosted productivity—in the early 1900s



to 50% more productive, estimates  
 man Behravesh, chief international  
 omist at DRI/McGraw-Hill. U.S. com-  
 es are major players in telecommuni-  
 ons, finance, and other businesses in  
 developing world. Exports to the Pa-  
 Rim, the world's fastest-growing re-  
 , account for 18% of total U.S. export  
 s, vs. 15.5% in 1990, according to DRI.  
 he gains in competitiveness have not  
 vented the U.S. merchandise trade  
 eit from ballooning to a record \$188  
 on, at an annual rate. In part, this reflects the powerful  
 and that Americans have for imported oil, cars, and oth-  
 roods. And there's ample evidence that closed or partially  
 ed markets abroad may dampen exports. Korea's auto in-  
 try thrives behind steep trade barriers. India is on strike  
 nst foreign capital. The mercantilist Japanese export to  
 world and protect their home market.  
 et the trend is toward more open markets and freer  
 e, as exemplified in the North American Free Trade  
 eement and the broadened General Agreement on Tariffs  
 ade. Out of the 16 most populous developing nations, 13  
 alized trade and foreign investment rules from 1980 to  
 3, according to Henry S. Rowan, professor at Stanford

## Unit labor costs are flat. During the 1980s, they rose by an average of **4.1%**

spite economic weakness in virtually all of its leading trading  
 partners. The industrial world's strongest economy, the U.S.  
 has been a magnet for imports. Still, exports are up by more  
 than 11% compared with a year ago, after adjusting for infla-  
 tion. "Considering differences in business cycles, if we hadn't  
 seen strong productivity growth and increased global compet-  
 itiveness, the trade deficit would be much worse," says Mark  
 Zandi, economist at Regional Financial Associates Inc. Over  
 the next several years, assuming world growth rates pick  
 up, the trade deficit could fall sharply.

Fact is, American companies are ahead of the pack because  
 of the openness of the U.S. economy. Business here has  
 lived longer than its overseas adversaries with red-hot com-

. From 1948 to 1973, produc-  
 e by 2.5% a year, and real  
 earnings gained 3%. When pro-  
 duction slowed to 0.9% a year from  
 1973 to 1980, wage gains slipped to a  
 0.5% annual rate. This relation-  
 ship is also true for Germany and Ja-  
 pan. Big wage gains in those coun-  
 tries coincided with rapid productivity  
 growth after World War II.  
 From one year to the next, wages

and productivity don't necessarily move  
 in lockstep. When Japan enjoyed an  
 enormous surge in manufacturing pro-  
 ductivity, starting in 1968, real compen-  
 sation did not catch up until around  
 1973. And in the U.S., it took several  
 years for the sharp productivity drop of  
 the late 1970s to trickle down into a  
 slowdown in real wage growth.

Wage inequality could also narrow  
 as America's high-productivity econo-

Moreover, software companies are mak-  
 ing their products more accessible to  
 the masses, even as computer learning  
 aids for the technologically illiterate  
 proliferate. "When a new technology  
 comes in, initially the better-educated  
 workers are better at adapting to the  
 technology," says Kevin Murphy, econo-  
 mist at the University of Chicago.  
 "But," he adds, "eventually, everyone  
 learns, and the premium for knowledge  
 falls back."

That's what happened at the turn of  
 the century. The introduction of type-  
 writers, addressing machines, dicta-  
 phones, mimeo machines, and other in-  
 novations made many office tasks  
 simpler to do, according to research by  
 Claudia D. Goldin and Lawrence F.  
 Katz, economists at Harvard Univer-  
 sity. At the same time, the percentage  
 of Americans with high school diplomas  
 rose sharply. As a result, the wage pre-  
 mium paid to white-collar office work-  
 ers fell between 1914 and the early  
 1920s, even while overall living stan-  
 dards were rising.

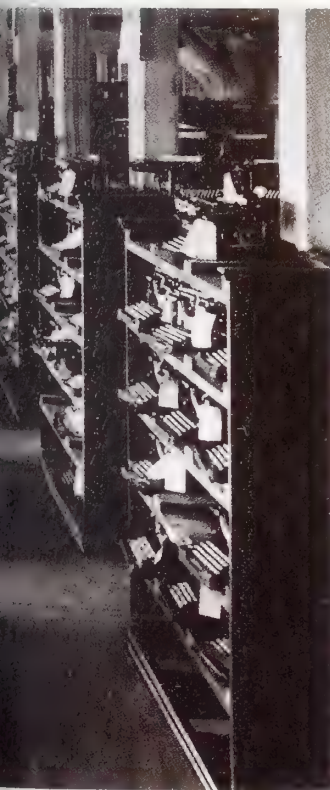
Cold comfort to a laid-off middle  
 manager or a worker who hasn't gotten  
 a pay raise in years. Still, today's high-  
 tech productivity bonanza will have a  
 double-barreled impact on living stan-  
 dards. It will raise wages as the coun-  
 try becomes ever more productive. The  
 march of the microprocessor will also  
 increase economic mobility as workers  
 upgrade their skills and move up the  
 earnings ladder. When the payoff  
 comes, the wait will have been more  
 than worth it.

*By Christopher Farrell in New York*

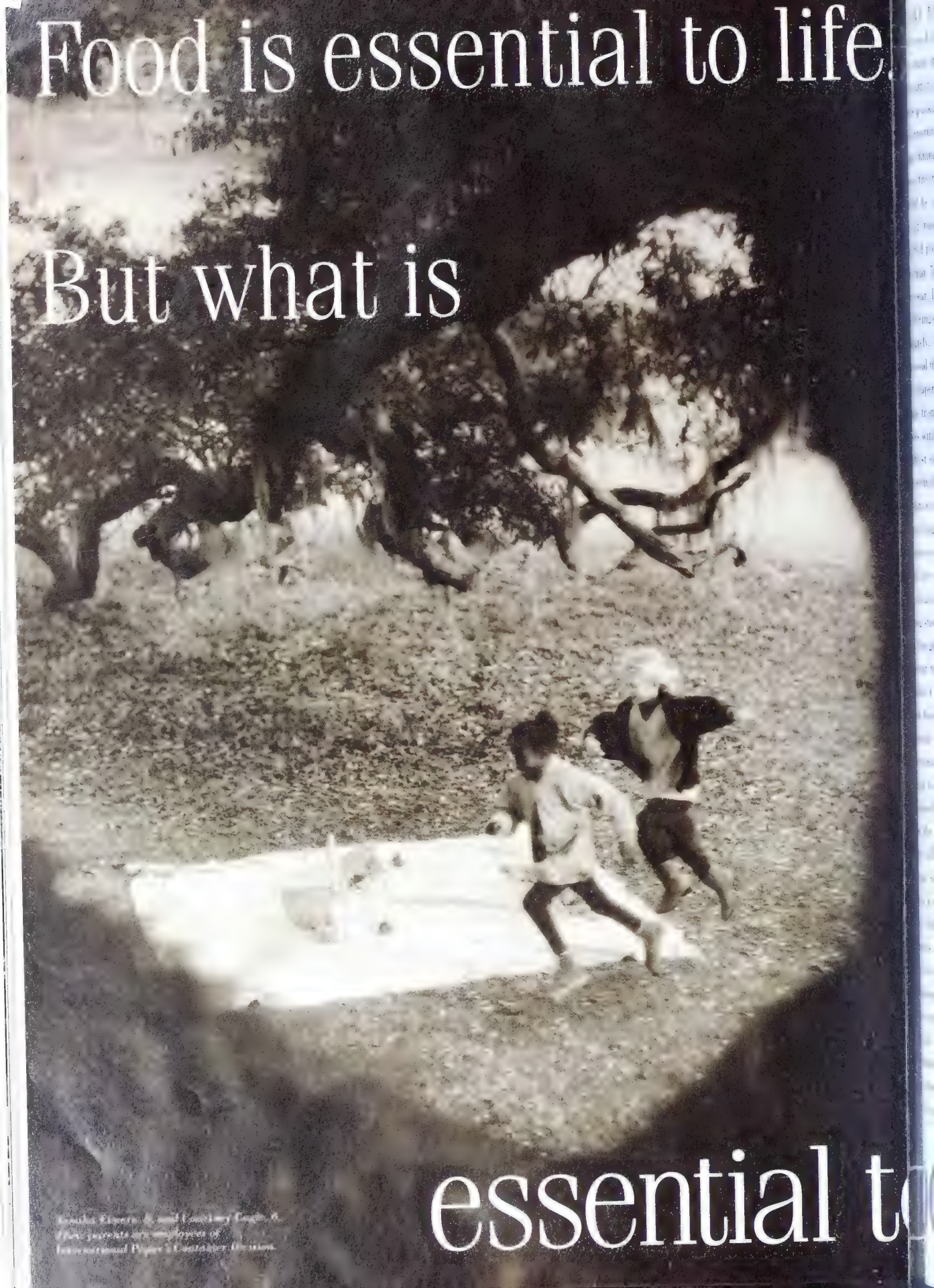
## As more workers gain skills, the premium paid to operators of high- tech gear will fall, but overall wages will rise

my kicks into high gear. Up to now,  
 companies have been paying premium  
 wages for skilled labor in this high-  
 tech era. For instance, employees who  
 use computers are paid on average  
 about 15% higher wages than those  
 who don't. The average annual earn-  
 ings of male college graduates are  
 some 70% higher than those of high  
 school graduates; at the end of the  
 1970s, the premium was 42%.

**"EVERYONE LEARNS."** Yet the skill level  
 of American labor is improving, with  
 more workers getting the education and  
 training employers require. A whole  
 generation is picking up skills at com-  
 munity colleges and technical institutes.







Food is essential to life.

But what is

essential to

*Journal of Food Studies*, 1994, 11, 1-10  
Food: a study in the history of  
International Food & Nutrition

## WHAT ARE THE ISSUES?

Just as our bodies need nourishment to make it from childhood through youth to adulthood, our food needs packaging to make it travel from the farm through the grocery store to our dining tables.

Without the right packaging, food would be wasted. Indeed, parts of the world lacking sophisticated packaging technology lose more than 50% of the food is produced every year. It either rots or is damaged during shipping.

Luckily, we have the technology to avoid these problems. For example, a paper package isn't just made from paper of varying thicknesses with graphics thrown on. Almost every package is a remarkable technological feat, each a unique solution to a special problem. Some packages endure fluctuations in temperature and humidity, hold ice while allowing the contents to drain, some withstand crushing stacking without being damaged. You get the idea. Without different types of packaging, we wouldn't have access to as much fresh food. You also wouldn't have as much variety. Some foods would become too expensive for most people to afford.

The abundance of packaging raises the question: would we be better off without it? The answer: not really. The practical answer is a packaging material that not only fulfills all the requirements of getting food to us but also is ecologically conscious, sustainable, renewable and recyclable.

At International Paper, we understand the need to find a balance between preserving milk for tomorrow's breakfast and preserving forests for future generations.

## WHAT WE ARE DOING.

International Paper invests millions every year developing innovations that keep food fresh and nutritious. Our Barrier-Pak® beverage cartons use a patented layering process of special papers and coatings that function as sophisticated barriers to hold in the fresh taste and flavor of juices. We're also working on new packaging systems that will keep milk fresh and nutritious even longer.

Along with creating revolutionary packaging, we're constantly looking for new ways to use less wood fiber in our packaging. One example is our Pineliner® technology, which produces corrugated boxes that require 17% less fiber yet remain as strong as conventional boxes.

We meet the need for virgin fiber through "sustainable forestry," which includes planting 50 million SuperTree™ seedlings every year. SuperTrees, developed through a process of natural selection, produce 30% more wood per acre over a 25-year growing period.

## WHAT IT MEANS TO YOU.

You can have fresh-tasting Florida orange juice in the dead of winter in Minnesota.

You can have fresh milk and tender chicken in Manhattan any time you please.

In short, you can have food that tastes as fresh as it does on a farm no matter where you live in America.

To talk more, please call Bob Gordon or Lyn Bernstein at the International Paper Packaging Innovation Center, 1-800-577-9862.

**INTERNATIONAL  PAPER**  
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# Food?





**ON TRACK:** Skill levels are high at Pitney Bowes, where a local community college helps train workers

have lowered their unit cost base by about 9% while European companies have done little or nothing," says S. G. V. burg & Co. chemical analyst Paul Raman.

Sputtering multinational giants such as Germany's Daimler-Benz, France's Alcatel Alsthom and Belgium's Soci t  G n rale face the unenviable task of slaying tens of thousands of jobs to improve efficiencies. Many of the Continental players in such leading-edge businesses as computers and telecommunications

competition. With the world's largest consumer market luring foreign rivals, battles for markets and profits have been relentless. With a government eager to deregulate, market forces have been unleashed in everything from telecommunications to electric utilities. With a society open to entrepreneurs, upstarts such as Bill Gates of Microsoft Corp. and Herbert D. Kelleher of Southwest Airlines Co. have shaken up industry after industry. "The more open U.S. market has forced American companies to be very competitive, both domestically and internationally," says David L. Blond, director, international trade forecasting at DRI. "American companies made the transition sometime around the mid-1980s, and they have embraced a competitiveness ethic much more than either German or Japanese companies."

**SMOTHERING.** Indeed, Europe Inc. is only now starting a painful restructuring. True, many European companies overhauled their operations in preparation for a single market in 1992, and competition is keener with the collapse of communism and the rise of emerging markets. But competition in Europe is still a far cry from what it is in America, and, for the most part, managements have a long way to go to get their organizations more efficient and their production costs down. Take the chemical industry. "American companies

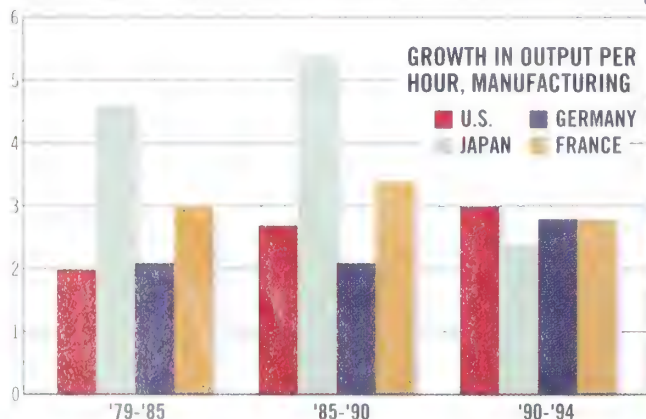
are smothering under interventionist government policies. European governments are still struggling to deregulate their airline industry nearly two decades after the U.S. did.

Japan, battered by the bursting of its 1980s "bubble economy" and the surging yen in the 1990s, is financially fraile. Even when its banking mess is cleaned up and the economy revives, many companies face years of paring employment. Despite first-rate multinationals, such as Toyota Motor Corp. and Hitachi Ltd., a surprisingly large number of Japanese industries are lagging their global rivals, a situation that is only worsened as Japan's economy becomes more service-oriented and information-intensive. "The Japanese are world-class in autos, consumer electronics, and a few other high-tech areas. Once you get beyond those industries, Japan is not very competitive or productive," says economist Behravesch.

Some economists are still skeptical that Corporate America's gains are durable. They believe the improvements only mirror the lower value of the dollar rather than advances in competitiveness. Worse, they say gains by U.S. companies have little to do with better living standards for the majority of Americans. Productivity is up. Corporate coffers are full. But worker paychecks haven't kept pace. After adjusting

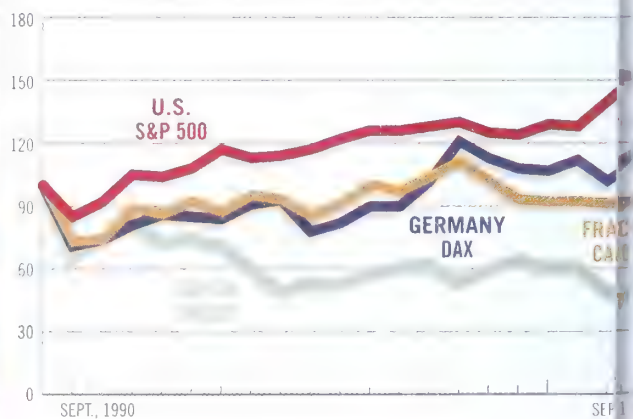
## The U.S. Moves Ahead in Productivity...

## ...and Its Stock Market Shines



▲ AVERAGE ANNUAL PERCENT CHANGE

DATA: BUREAU OF LABOR STATISTICS



▲ INDEX: JUNE 1990=100; NO DIVIDEND REINVESTMENT

DATA: BLOOMBERG FINANCIAL MARKETS



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inflation, wages have been stagnant in the 1990s.

But this widely shared outlook is much too gloomy. A stronger dollar could pinch profits at multinationals such as Gillette Co., which had 68% of its sales overseas last year. Yet adjusting for both the domestic and global business cycles, improvements in U.S. productivity have been twice as important in explaining U.S. export performance as the changes in the value of the dollar since 1991, says economist Zandi. Currency is not the story. It's productivity.

What's more, if history is any guide, sustained gains in productivity eventually translate into higher living standards (page 116). It took time for management and labor to learn how to use the new technologies. Now, the productivity gains are clearly emerging, and incomes will follow. This doesn't just mean higher wages, though that's a big part of it. Faced with a fearsome competitive environment, companies are offering higher quality goods and services at a lower cost, which also boosts living standards. "Forget price increases," says Southwood J. "Woody" Morecott, CEO of Dana Corp., a \$6.6 billion auto-parts maker. "The only way to improve your margin today is by improving your product."

The evidence from a wide range of industries shows that the productivity gains are real and ongoing. Whether it's manufacturing semiconductors, offering banking services, or keeping track of medical records, U.S. companies are doing more with less. GTE Corp.'s operations in Florida's Tampa-Sarasota region is more the rule than the exception. Over the past five years, the area's population and telephone system have grown by about 7% annually, yet GTE still employs the same number of service people, about 250. Laptops let repair crews plan their daily schedules efficiently and allow customers to get a more accurate time of arrival from the repair folks. The staff backing up these technicians has dropped from 45 to 11 as software-driven "expert" systems take

The U.S. stock market is up **75%** since 1990. Japan's market has plunged by **50%**

should continue to invest. "It all really points to a period of fairly low inflation and higher-trend productivity growth than we've had for a couple decades," says William Sterling, managing director at BEA Associates, a management firm in New York City.

Of course, the world isn't standing still. Managements in Europe and Japan are grappling with their problems, and developing nations such as South Korea and Taiwan are coming on strong. That's why U.S. companies are now taking interest in their human capital—their workforce—more seriously. When mass production ruled, competitive advantage lay in fragmenting work, highly specialized tasks, and managing via hierarchical bureaucracy. What's different today is that productivity gains, in an era of computer and communications technology, increasingly rely on delegating authority and organizing workers into self-managing teams.

As in any dramatic conversion, a lot of companies



**HIGH-TECH PUNCH**  
Motorola and other U.S. chipmakers are boosting productivity—and investment—leading

stumbling as they gear up for a more flexible, responsive corporate structure. Reengineerings and restructurings have been just management speak for massive layoffs without any transformation of work. Shattering of bureaucracy. Surveys by consultants and academics show companies cutting too deeply into workforces and reluctant to delegate sufficient authority.

Nevertheless, t

signs point toward more and more companies trying to change. Look at DuPont Co. It has gone through a wrenching two-stage restructuring since 1991. In round one, jobs were slashed in middle- and upper-management ranks, and employee morale plummeted. Round two was also distressing. Senior management split the company into some semiautonomous business units aimed at flexibility and reactivity. Financially, the maneuvers have paid off. Last year earnings rose by 65%, excluding extraordinary charges. And employees, the turnaround is palpable. Says Edward A. Riley, a 25-year veteran and manager of corporate training and education: "I find it liberating. You have the freedom to go out and make changes and make things happen. You don't have to ask permission." Adds Michael J. Fradette, director for manufacturing consulting at Deloitte & Touche: "To do more money in a disinflationary period takes real innovative creativity at all levels of the corporation."

Companies are also putting more effort into preparing workers for the new world of work. Formal company training increased by 45% from 1984 to 1993, according to Antonio Carnevale, director of human resource studies at the Council

## Cover Story

Brynjolfsson and Lorin Hitt of Massachusetts Institute of Technology found evidence in a survey of nearly 400 companies that the return on investment in information systems could exceed 50%.

**TEAMWORK.** Investment spending is remarkably robust, too. Outlays for producer durable equipment as a share of nominal GDP is 8.2%, compared with 6.5% in 1991. With prices for computers and office machinery falling by 13% a year over the past half-decade and the sustained rise of the U.S. stock market attracting billions in new capital, companies

customer requests and arrange them in the most efficient order. Professor Erik

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tee for Economic Development, a think tank in Washington, D.C. For example, Dana Corp. has doubled the time and money it spends on training and education programs over the past several years. "We're teaching people to look for ideas," says CEO Morcott. "A lot of the education is on how to spot ways to improve our business." In general, corporate training programs tend to favor technical workers and managers, but a study by Ann Bartel and Nachum Sicherman, economists

at Columbia University, found that in industries with high rates of technological change, employers do compensate for workers' lower levels of education by providing more training.

Then there's the experience of Pitney Bowes Inc., the world's largest maker of postage meters and mailing equipment. Nearly five years ago, the Stamford (Conn.) company collaborated with a local community college to devise a customized seven-stage training curriculum. In a manufacturing

setting where more than 17 languages were spoken, about 40% of its 1,500 pro-

duction workers were not literate to the required minimum of fourth-grade level, and 65% required some kind of math training. Today, almost everyone meets the basic literacy and math requirements, and employees spend several hours a week in training sessions developing other skills. Employees now work in teams, collaborate with engineers, order materials, and monitor product quality. Says Kevin Connolly, director of systems-products manufacturing: "These workers have

The U.S. has  
**63** PCs per  
100 workers. In  
Japan, the figure  
is only **17**

economist at Cornell University. New entrants to the job market are considerably better educated than workers retiring from the labor force.

At the same time that more people are getting the education and training employers desire, information technologies are increasingly user-friendly. All of the major computer and software companies are developing programs that blur the distinction between expert and novice. "Up until the early 1980s, the only people able

to use personal computers were a very tiny elite. Now, a lot of software is for numbskulls. In some sense, the technology is democratizing rather than elitizing," says David Card, economist at Princeton University. Adds Sharyl Schubert, a hairdresser in Chicago who recently bought an Apple Macintosh computer for her 4½-year-old daughter, Jessica: "I don't think the emphasis on computers is going to be divisive for American society. I think they are going to be part of normal life, and right now, we're in the transition. There are computers everywhere—Marsell Field's, restaurants, even my Dad's pharmacy."

**PAINFUL UPHEAVAL.** Adam Smith was right. There is a great deal of "ruin" in a nation. The dynamism of capitalist competition is devastatingly painful. While 18th century textile makers in Britain built the factory system, middle-class weavers in Yorkshire sank into poverty. In the 1800s the spread of railroads devastated communities without a rail link. The 1950s and 1960s were an era of U.S. economic dominance, but many industrial laborers never recovered from losing the well-paying manufacturing jobs that thousands of them held before industrial companies moved from

## Cover Story



### "DEMOCRATIZING":

User-friendly software and training guides are making computers accessible to all

the Northeast and Midwest to cheaper sites in the South and West.

Today, high school dropouts and less skilled workers confront troubled times. With a world economy more competitive than it has been in at least a century, everyone—the educated and the uneducated alike—faces insecurity and earning instability. That is, all of society's major economic institutions—from businesses to schools

and homes; they make decisions all the time. Yet in the past, we treated them as if they were incapable of making decisions when they came into the factory. No more."

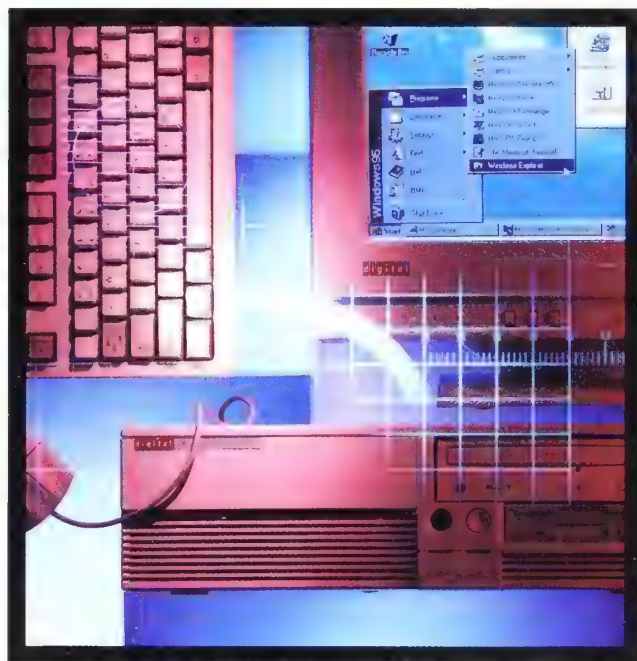
Like any market, be it oil or stocks, wages are sensitive to the ebb and flow of supply and demand. For more than a decade, those with a college education or technological skills have been well-paid while everyone else stagnated. The U.S. workforce is heeding the market's message. The percentage of high school graduates enrolling in college after graduation jumped from 49% in 1980 to 62% in 1992. The ratio of bachelor's degrees awarded to those 18 to 24 years of age rose a remarkable 29% from 1980 to 1990, according to John Bishop,

government—are under increasing pressure to do more with those ill-prepared to compete in the new economy and cushion workers against income fluctuations.

Nevertheless, the nation's economic vitality is being restored. Many U.S. industries, from telecommunications to Wall Street, are genuine global competitors. The lesson of history is that given time, the productivity bounty that has been largely confined to corporate coffers will be shared by all Americans—improving everyone's standard of living.

By Christopher Farrell, with Michael J. Mandel in New York, Joseph Weber in Philadelphia, and bureau reports

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# INTEL UNBOUND

Its move into computer design is forcing the entire industry to march to its beat

**T**ap-tap-tap-tap-tap-tap. David House, a senior vice-president at chip giant Intel Corp., raps out a precise staccato beat with his knuckles. What you're hearing, he says, is the racing heartbeat of an industry. "Twice a second," House explains, "somebody buys an Intel-based computer."

As astonishing as that pace is—some 55 million Intel-powered personal computers will be sold this year, a 30% leap over 1994 shipments—it's not good enough for House's demanding boss. Chief Executive Andrew S. Grove has already built Intel into an \$11.5 billion powerhouse: the biggest and richest chipmaker in the world. Its microprocessors now chug away in 150 million PCs, and, because Intel chips are being designed into all sorts of systems, "80% of all computing in the year 2000 could be done using Intel technology," predicts Gartner Group analyst Mark Specker. Still, Intel's hard-charging CEO is pushing to create even greater demand.

Grove's motivation is simple, and the voluble executive has been perfectly upfront about it: To support the huge—and growing—costs of developing and building microprocessors, Intel needs to generate huge profits. The company now spends approximately \$1 billion to design a microprocessor and then plows \$1 billion into each plant that builds it. There are two ways to cover that nut: One is to create new demand for PCs. The other is to preserve high profit margins by accelerating the shift from one generation of microprocessors to the next. That makes it harder for clonemakers to catch up and force Intel to cut prices ahead of its schedule.

**PERSONAL JITTERS.** About four years ago, Grove hit on a formula to achieve his goals. While the Pentium was in development, his long-simmering frustration with the slow evolution of the IBM-compatible PC "platform" boiled over. The guts of most PC clones—aside from the microprocessor—had not advanced far beyond the 1984 IBM PC/AT. Grove worried about losing ground to other plat-

forms, such as Apple Computer Inc.'s Macintosh or even Sun Microsystems Inc.'s SPARC designs. Sluggish development was also helping Intel cloners grab market share. Grove feared for the success of the Pentium generation—on which he was betting \$5 billion in development and production costs.

So he put Intel into the business of designing computers. Instead of launching the Pentium chip and then getting computer makers to design machines around it, a process that could take a year, Intel began doing the job itself. It figured out the "chip set"—a collection of logic semiconductor chips that surround the microprocessor and perform functions such as synchronizing the actions of various components. And it greatly stepped up efforts to design and build entire motherboards, the circuit cards at the heart of PCs. When Pentium went into production, Intel also started selling chip sets and motherboards. Soon, dozens of PC makers were selling Pentium machines.

For Intel, the formula is working beyond all expectations. Not only is it pushing its own chips out faster—Pentium's successor is due out in November, before Pentium clones have appeared in volume—it is also using its motherboards and chip sets to speed to market a host of improvements to the PC, including a faster "bus" for moving data in and out of the computer. That has helped push PC demand beyond analysts' forecasts and has put Intel on course to exceed \$20 billion in sales by 2000.

It has also made Intel arguably the most powerful force in industry—a mixed blessing at best for PC makers. Much as they enjoy the current PC boom, they worry that their industry is being hollowed out and that they are ceding unprecedented power—and riches—to Intel. While the chip giant gobbles up more pieces of the PC, computer

makers are finding fewer ways to differentiate their products and relieve the margin squeeze that has lately let up since the price wars of the early 1990s (charts). "Everybody's been hassling Gates about Microsoft monopoly," says the chairman of a computer maker. "Microsoft doesn't

Grove has accumulated such Gatesian leverage that rivals hesitate to even discuss it on the record



leverage that Intel has today." strong is Intel's influence? One the reluctance of computer executives to talk about the chipmaker's on the record. A year ago, Com-puter Chief Executive Eckhard blasted Intel's strategy at a con-ference. He railed against Intel's grow-er and, in particular, its mother-board business, which helped rivals like 2000 Inc. and Dell Computer bring out Pentium-based machines of the Houston-based giant.

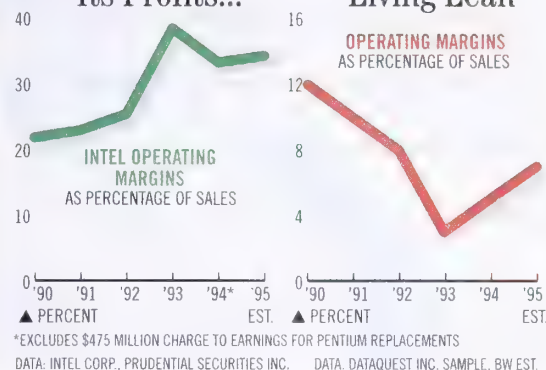
**BANDWAGON.** This year, Pfeiffer changed his tune. When the next-generation Pentium Pro chip (code-named P6) comes out in November, it will be among the PC makers to market with machines based on Intel motherboards. He'll be in good company: IBM, Digital Equipment, Compaq, and a host of others do the same. "If you want a PC in the fall, you have one choice," says a PC executive at a

major computer maker. "You buy the Intel box because they're doing the chip, the board, the mechanicals, everything."

Intel's new game plan is shaking up the entire PC industry, toppling some leaders and crowning new ones. Hewlett-Packard Co. has made a smash reentry into the PC market, vaulting into the top 10 in only two years, partly by using Intel motherboards. Its first consumer PCs, which came out last spring, were built entirely by Intel. Digital, another comeback kid, relies on Intel motherboards for a quarter of its machines, and home-PC giant Packard Bell Electronics Inc. relies on Intel for most everything it sells.

AST Research Inc. is the latest major PC maker to get with the program. The Irvine (Calif.) company announced on Sept. 11 that it will post a larger-than-expected loss this quarter because Packard Bell, Gateway 2000, and other Intel motherboard customers had beaten it to market with new models. "Intel has changed the

## While Intel Fattens ...PC Makers Are Living Lean Its Profits...



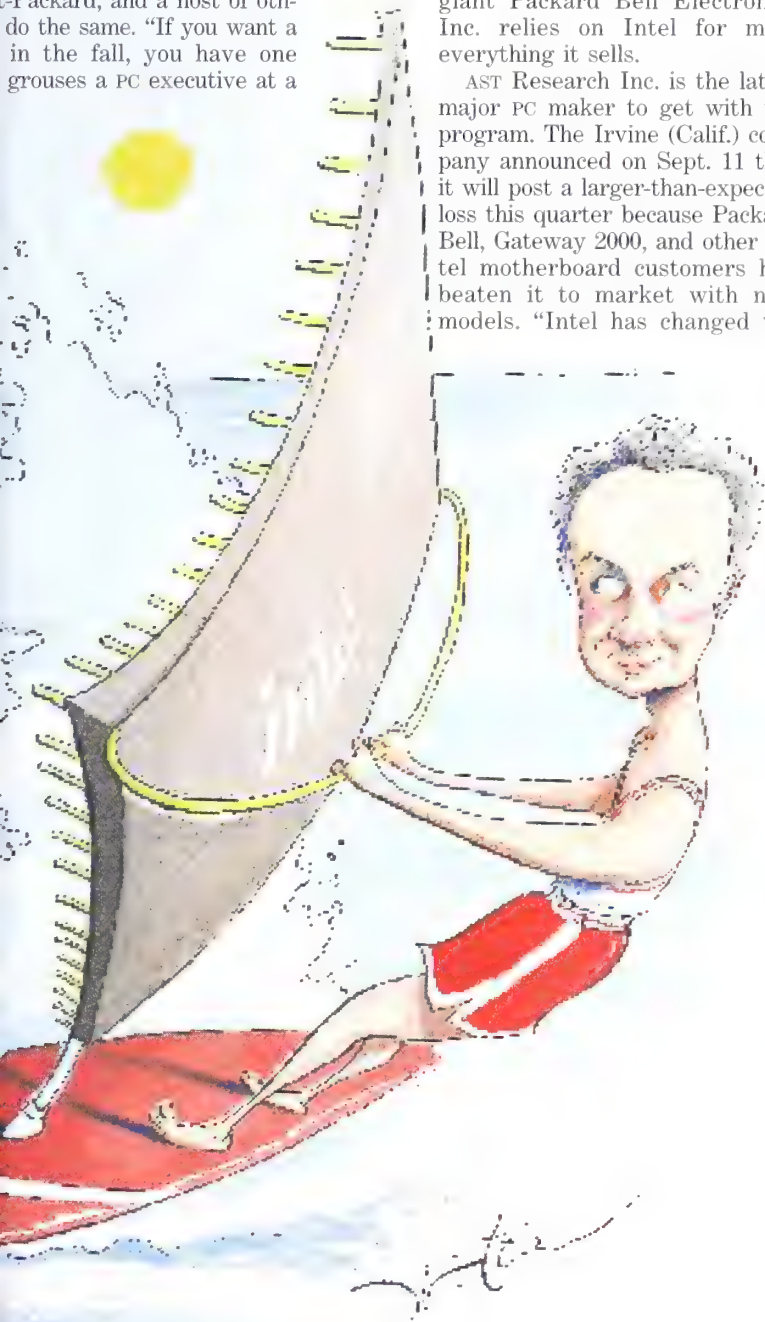
business," says Safi U. Qureshey, the chastened chairman of AST. "A few years ago, our focus was the addition of unique [hardware] features as differentiators. But getting to market fast with the right configuration is better than showing up three to six months later with our own gee-whiz feature."

The solution: join the growing ranks of Intel motherboard customers—then scramble to come up with a marketing message, package design, or software that will make your product stand out in a sea of identical hardware. The sad reality, says Leslie Fiering, vice-president of market researcher Gartner Group: With an Intel motherboard, "even the mom-and-pop store down the road can do a PC that rivals Compaq's."

No wonder, then, that in just three years, Intel has become the world's largest producer of motherboards. It's expected to sell 10 million boards this year and twice that next year. This makes Intel a huge buyer of components such as chips, further complicating the lives of PC makers who want to build their own boards. One reason for AST's nosedive, Qureshey says, is that it was waiting 16 months for components that it could get almost immediately if it bought them on boards from Intel. The growing Intel motherboard empire is also wreaking havoc in Taiwan (page 154).

**BULLETPROOF MARGINS.** By controlling the motherboard business, Intel not only sets the pace of technology, it also can set prices—while still protecting the margins on its cash-cow Pentium chips. If it cuts prices on motherboards, the whole industry has to follow, reducing PC prices and making them more attractive to buyers. Intel reaps the benefit of those higher sales without slashing prices of Pentiums, which carry 70%-plus gross margins.

It's not surprising that PC makers have the willies over what Intel might do next. Their biggest worry: The chip giant will follow its massive Intel Inside brand-identity campaign with an



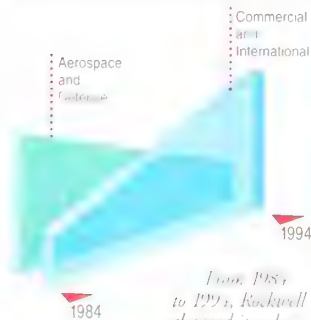


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Intel Outside offensive. That means building Intel-brand computers. Grove swears he'll never do that because his customers know how to sell finished PCs better. But he doesn't rule out making more complete systems for others to sell if that proves the best way to move chips. On Sept. 15, Intel tilted that way, announcing plans to spend at least \$100 million on a plant in DuPont, Wash., that will crank out complete systems for PC makers to resell. "Intel could flip a switch and become the largest system vendor in the world," says Robert N. Gunn, sales and marketing vice-pres-

up of PC makers such as Compaq and IBM and chipmakers such as Cyrix and Advanced Micro Devices, hopes to develop a basic PC design not tied specifically to Intel chips. It's also working on its own bus and multimedia standards. Snaps one angry PC executive: "If I had an alternative, I would run."

Trouble is, there isn't much of any place to go. NexGen Inc. has a Pentium alternative, but it doesn't have the Pentium's built-in math circuitry and requires a special PC design. Cyrix Corp. and AMD are both late with Pentium-class chips, and on Sept. 26, AMD

uses a single type of connector to all peripherals like printers and modems. The Hillsboro gang also has schemes for running video on computer networks, and they've built lightning modems to grab data sent over cable systems. "We either deliver something that's going to appeal to the next million people who want computers, or to the next 50 million who want to replace their computers with something else, or we won't grow," says Grove.

For all its muscle, Intel doesn't always get its way. Its ProShare video conferencing setup has been slow

## Making More PCs Now, But Enjoying It Less

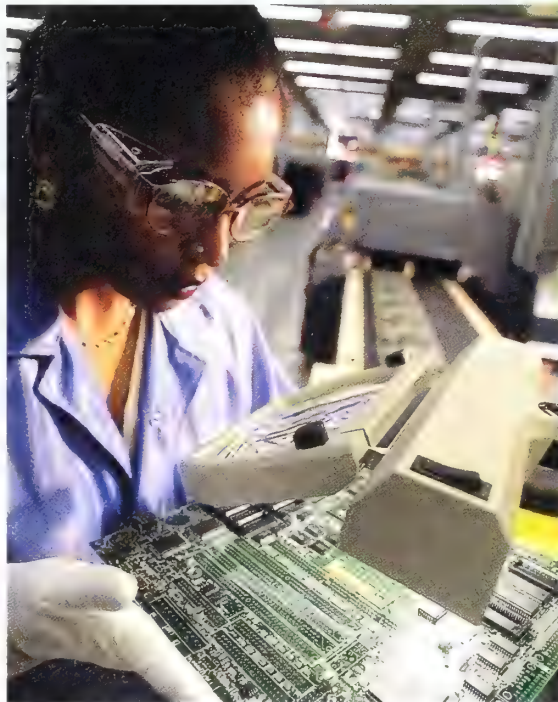
**1985** A decade ago, major PC makers designed and built much of the guts of their machines. They bought disk drives, monitors, power supplies, and chips from outside suppliers. But they usually designed their own motherboards, graphic chip sets, disk-drive controllers, and BIOS (key software to make a PC IBM-compatible). Intel's contribution: chips, mainly microprocessors.

ident at Micronics Computers Inc., a motherboard maker.

Meanwhile, the chipmaker is expanding its design work beyond desktops. When it brings out the Pentium Pro, it will also trot out a design for a network server based on the new chip. Servers, the computers that anchor local-area networks, have been among the few remaining high-profit niches for PC makers and have helped server leader Compaq make up for slim margins in home PCs. Come November, however, Compaq will be selling a Pentium Pro server designed by Intel.

The more Intel does, the less PC makers can do themselves. It's a vicious cycle: Unable to differentiate their hardware, PC makers will compete on price, leaving less to invest in new technology and rendering them even more reliant on Intel. Even Compaq, which still strives for hardware differentiation, has scaled back its R&D budget from as much as 6% of revenue to around 1.8%. "We still see an ability for us to do value engineering," says Ross Cooley, a Compaq senior vice-president.

Some PC makers are quietly plotting ways to get around Intel's dominance. A secretive group called Sundance, made



**BIRTH OF A MOTHERBOARD:** All-Intel inside

said its K5 won't be out until mid-1996.

Apple's Mac design, based on the Motorola-IBM PowerPC chip, is a possibility. "Intel is stealing the board business, so boardmakers will be happy to go to a different standard," asserts Apple licensing director James S. Gable. But there are few converts, perhaps because an Apple-IBM "common reference platform" board won't be out until next year.

That pretty much leaves Intel in the driver's seat—with its foot on the gas. In Hillsboro, Ore., Intel Architecture Laboratories is busy creating hardware and software to transform the PC into the Swiss Army knife of the Digital Age, an all-purpose multimedia, video-conferencing information appliance. One innovation, the Universal Serial Bus,

**1995** Only a few major PC makers, such as IBM and Compaq, still make motherboards. But because they can't produce a motherboard design as quickly as Intel, even these giants are relying on the chipmaker for their first Pentium Pro-based machines. Intel's contribution: microprocessors, motherboards, chip sets, complete PCs, software.

DATA: BUSINESS WEEK, INDUSTRY ESTIMATES

take off because of high prices and jerky video. And in August, Intel's newest PC initiative, Net Signal Processing, stalled. Intel hoped to persuade software developers to back the scheme, which would allow PCs to run sound and video on Intel microprocessors. That way, PCs wouldn't need graphics and audio cards but consumers would have more reason to buy models using the fastest, most profitable Intel chips. But

Intel didn't write the software to work with Microsoft's new Windows 95 operating system, so Microsoft warned software developers to avoid it. Result: Intel will relaunch the initiative next year.

NSP revealed a hubris that has plagued Intel. The scheme would have inserted a layer of software that would allow video and audio signals to preempt Windows. "NSP's a bad Intel thing," says Carl Stork, director of Microsoft's Windows hardware programs. "It doesn't mean it's on Microsoft's road map." Concedes Grove: "We screwed up on NSP. At times, we advocate more than we listen."

More and more, however, the industry listens—and follows. And, privately, PC makers concede that v

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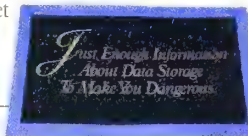
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Grove's strategy may have given Intel immense new power, it has also produced a market boom that is helping all of them.

Can Grove's speedup last indefinitely? Can PC makers figure out how to prosper under the conditions that the chip giant is imposing? Grove says the two issues are inextricably linked: As long as he can keep the industry humming, PC

makers will find ways to make hay. Of course, not everybody buys the scenario. Wall Street, for example, discounts Intel's prospects. Although the stock has more than doubled since last October, at around \$60 it is more than 20% off its 52-week high and trades at only 14 times projected earnings. The chief worry: Intel won't maintain its margins and earnings momentum.

Grove's answer is to keep up the relentless pace. "If the end-user gets satisfied with the PC that the industry produces," he says, "we are going to be in Hurt City." Little chance of that as long as Andy Grove is keeping the pace.

*By Robert D. Hof in Santa Clara with Larry Armstrong in Los Angeles and Gary McWilliams in Houston, and bureau reports*

## TWO OF TAIWAN'S MOST HATED WORDS: INTEL INSIDE

**J**ust a few years ago, Taiwan's electronics industry was buzzing. Computer companies from around the globe were buying its motherboards, components, and finished PCs. In 1990, approximately 100 Taiwanese companies were cranking out motherboards—the guts of computers that would later be sold by Dell Computer Corp., Gateway 2000 Inc., and dozens of other brands in the U.S. and Europe. Taiwan produced 60% of the world's motherboards. Now, only 20 companies have managed to survive an industry shakeout.

Things are about to get worse. Sales grew 11% in the first half, but boardmakers are girding for a crunch. The Institute for Information Industry (III) predicts that the situation could be so severe that shipments will only edge up by about 5%, to 12 million boards, for the year.

Ask anyone in Taipei's sprawling electronics community, and they'll name the culprit: Intel Corp. As the chip giant has pushed aggressively into the motherboard business, life has become more difficult for Taiwan's boardmakers. "I believe that Intel will have a direct impact on Taiwan's motherboard performance in 1995," says C.S. Ho, chairman of the Taipei Computer Assn.

**SLOW MAIL?** Boardmakers aren't the only ones who worry about Intel's expanding role in computer making. Companies that make chip sets—the logic chips needed to make a computer "IBM PC-compatible"—also feel the effects. Acer, the \$3.2 billion giant of Taiwanese electronics, has been a

leading player in chip sets but says it was unable to come out with its second-generation Pentium set, Aladdin II, until June of this year—months after Intel introduced its equivalent chips—partly because it did not get specifications from Intel

mal complaints from chip-set makers. However, Taiwan's Fair Trade Commission is investigating licensing contracts with PC- and boardmakers that discouraged use of clone chips by forcing certain patent-royalty fees if the manufacturers used Intel micro-

processors but demanding them if they used clone chips.

Intel firmly denies any such allegations. "We abide by the law," says Alter, adding that its employees undergo rigorous training in antitrust issues. Intel also points out that Advanced Micro Devices Inc. and Cyrix Corp. have resolved concerns over this issue.

**"VERY NERVOUS."** Taiwanese computer executives insist that Intel is leaving them out. The big American company used to share information and enlist their



**TAIPEI PLANT:** Once a partner, Intel has become a rival

as early as it had with past generations of microprocessors. Chin Wu, president of Acer Laboratories Inc., which designs and builds chip sets, will not disclose Aladdin II's production figures but says its market penetration is much lower than he would hope by this stage.

Intel insists that it is maintaining a cooperative relationship with customers such as Acer, but the company acknowledges that as it shortens product cycles, it is forced to work with fewer partners and take less time to consider their comments. That does not mean quashing the competition, Intel says. "We grow best by growing our own business, not by taking away from others," says Karen Alter, Intel's director for strategic communications.

Intel has not encountered any for-

support so that they could help build volume quickly. "That changed as Intel upped its own production of chip sets and motherboards," says Colly Huang, deputy director of III's Market Intelligence Center. "Taiwan companies became very nervous this year when Intel tried to compete for orders from top PC vendors," he says.

With the dawning of the Pentium Pro era, Taiwan is watching to see how the chip giant proceeds. In August, Intel briefed Taiwanese manufacturers on the ATX motherboard that Intel will introduce with the new chip, and now, the Taiwanese companies are scrambling to come up with their own versions. However, they are increasingly leery of the new rival that used to be their old partner.

*By John Winzenburg in Taipei*

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<sup>1</sup>*Kiplinger's Personal Finance Magazine* measured the volatility of 118 general international stock funds for the one-year period ended 7/3/95 on a scale of 1 (least volatile) to 10 (most volatile). Volatility is based on standard deviation of total return. <sup>2</sup>Lipper Analytical Services, Inc. rankings and fund performance figures are based on total return, including reinvestment of dividends and capital gains for the stated period. Lipper ranked Janus Worldwide Fund #11 out of 108 global funds for the one-year period ended 6/30/95. Past performance does not guarantee future results. Your return and principal value will vary, and shares may be worth more or less at redemption than at purchase.

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EDITED BY AMY DUNKIN

## WHEN TO CRACK YOUR 401(k) NEST EGG



**E**ver look at the tidy sum you've accumulated in your retirement plan at work and daydream about what you would do with all that money if it were sitting in your bank account? In truth, you probably have access to some of the stash

through the loan provision in your plan. The question is: When is it worth tapping into?

Although 401(k) plans are first and foremost for retirement savings, about 70% of companies currently allow employees to borrow from the plan, and the percentage

### BORROWING

is rising, according to Access Research, a Windsor, Conn. marketing consulting firm. Most companies don't place any restrictions on how you use the money and offer favorable interest rates. Employees are allowed by law

to borrow no more than 50% of the vested amount in their accounts, which serves as collateral, up to \$50,000. Except for a loan to purchase a primary resi-

dence, which you can repay over 20 or 30 years, you have five years to pay back money you borrowed through automatic payroll deduction.

Although plan sponsors could impose stricter rules on lending, the current trend is for employers to make loans easier and quicker to get. That's partly because of strong demand from strapped younger employees who need the funds for more immediate goals, such as retirement, such as paying tuition or purchasing a home. But studies also show that lower-paid employees participate more in plans when loans are permitted—and, under fee rules, that has the corresponding effect of allowing highly paid executives to take away a greater percentage of their pretax dollar 401(k)s. About 20% of participants in plans that allow loans have at least one outstanding at any time. The share will probably climb as the amounts invested grow over time, since the returns will prove more tempting to tap, says Robert Wuelfing, Access' president.

**PHONE LOANS.** If you need to borrow money, turning to your 401(k) plan is relatively painless. For most large plans, the process is automated: All you have to do is call the toll-free voice-response system, press some keys, and a check is in the mail. By signing the back of the check, you agree to the loan conditions. There is no requirement, since the funds in your account serve as collateral. Some plans charge a monthly loan-initiation fee and



an annual processing of the costs and hassles typically minimal compared to going to a bank.

Interest rates are usually low. Retirement plans are required to charge market rates, usually prime (now plus one or two percentage points). That means

you'd currently borrow from your 401(k) at a 10% rate—a lot higher than the 18% credit cards charge. It's more than new cars or home equity credit.

Like any other type of loan, you pay the interest to yourself. So, if you take out a loan, taking out a loan doesn't stop your retirement kitty from growing. Even if the loan would have reduced an average of 10% paid back over 10 years at 10% interest, your account would grow almost as fast.

As always, there is a downside. Most plans require that if you leave or quit your job while you have a loan outstanding, you have to pay it back immediately. "In these times of downsizing, that's a real risk," says Melvin Borleis, a managing director at benefits consultant William M. Mercer. Most people who take out loans don't have the cash on hand to repay on short notice. "If you don't have the cash to pay back or you can't get the cash back, your employer is bound to report it to the Internal Revenue

Service as a withdrawal from the plan," says Robert Stone, senior vice-president of Retirement Services. The IRS triggers 20% withholdings, plus a 10% penalty if the IRS imposes on you contributions taken by participation under age 59%.

It's a big bite can that you can't? Borleis describes the scenario: A young executive with \$100,000 in his retirement account decides to

pull out \$50,000 for a luxury car. A few months later he's laid off and cashes in his plan to cover bills between jobs. After \$50,000 goes to pay back the loan, and \$20,000 is withheld for income taxes, he actually gets a \$30,000 check from his employer. Come tax time, he must come up with \$10,000 to cover the penalty

## Three Scenarios for 401(k) Withdrawals

*Three 35-year-olds have \$40,000 invested in a 401(k) plan that is growing at an average rate of 10% a year.*

*Assuming none invests any more money, here's how their actions could affect their nest eggs:*

### INVESTOR #1

Leaves the money in the plan, accumulating interest. By age 65, she has accumulated a tidy sum of \$698,000.

### INVESTOR #2

Borrows \$20,000 from his plan and pays it back with 7% interest over five years. Thirty years later, the loan has hardly nicked his savings: The plan is worth \$689,000.

### INVESTOR #3

Borrows \$20,000 from the plan only to be laid off from his job two months later, forcing him to cash in his 401(k) to pay bills. The employer uses \$20,000 to pay off the loan, withholds \$8,000 to cover taxes (20% on the distribution of the full \$40,000), and hands \$12,000 to the cash-strapped employee, who must pay a \$4,000 early-withdrawal penalty. He ends up with \$8,000 in cash and no retirement savings.

DATA: WILLIAM M. MERCER INC.

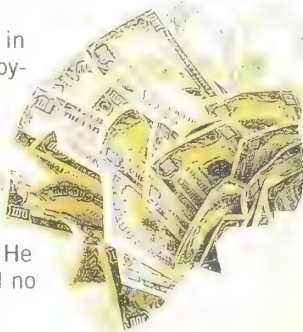
tax on the full \$100,000. Even once he finds another job and starts building another retirement fund, "his total amount available for retirement will be seriously diminished," says Borleis.

That's why Borleis says the first rule of borrowing from your 401(k) is: "Only take out a loan if you think you are secure in your job." You should use the money to cover the cost of something you would borrow to pay for—a

car, a house, tuition. Too many people borrow from their plans to obtain luxury items they couldn't otherwise afford, says Bob Hammond, author of *Life Without Debt* (Career Press; \$14.99).

In fact, the third most common reason people take out a 401(k) loan, according to Dreyfus, is to fund a vacation. The top two reasons, paying tuition (30%) and buying a new car (15%), seem more appropriate, says Hammond. It can sometimes make sense to borrow from a 401(k) to reduce the amount of high-interest credit-card debt you're carrying; the danger is that you will just run up the credit cards again. "Trying to borrow your way out of debt, you generally put yourself further into debt," warns Hammond. "Don't let this be a step toward bankruptcy."

Before you call your plan sponsor, shop for the best loan terms. While a 401(k) loan is usually better than credit-card debt, a home-equity loan is of-



ten more attractive. Since interest on a mortgage is tax-deductible, an 8% line of credit equals about a 5% interest-rate charge.

Once you've settled on a 401(k) loan, you need to consider some hidden costs. Even though your retirement plan earns the interest, it probably would grow faster if the money was invested in stocks. If the five years you borrow turn out like the last five in the stock market,

you'd miss out on an average annual return of 15% for the Standard & Poor's 500-stock index. Plus, while you do get the interest back, it is taxed twice; first, when you pay back the loan using after-tax dollars, and second, when you withdraw the funds. That's because the interest you paid yourself is considered earned income to your plan.

**TAX TOLL.** But if you really need the money before you turn age 59½, borrowing from your 401(k) plan is a far better option than simply withdrawing money early. You can secure a so-called hardship distribution to purchase a primary residence, fund education, pay medical expenses, cover the costs of a funeral, and avoid eviction or mortgage foreclosure. But you still have to pay income taxes on the distribution as well as the penalty tax for early withdrawal.

A philosophical debate is raging over whether allowing so many people to borrow against their retirement funds is a good thing. Many pension consultants and consumer advocates believe individuals should be forced to save for retirement separately from other goals. "The savings rate in this country is atrocious to begin with," says Access' Wuelfing.

"What saving is going on should be for retirement." But it is also argued that borrowing from a 401(k) is the only way many younger families can meet major expenses. "Today's worker is going to borrow," says Borleis. "It's just a fact."

If you do tap your 401(k) you should only do it once, says Hammond. While taking out one five-year loan has little impact on your ultimate retirement savings, making a habit of it could cost a bundle in lost investment gain. And, make sure the loan is worth the risk. If you need to tap your retirement funds for a trip to Disneyland, you should probably just stay home.

Amey Stone





**STITCH IN TIME:** Service can be lightning-fast

## HONG KONG TAILORS SUIT WOMEN, TOO

**Beth Ann Felshman** rushes into the Margaret Court Tailoress Co. in Central Hong

Kong. It's Monday, she's getting married on Thursday, and today proprietor Margaret Wong is doing the final fitting on the cream-colored suit that Felshman will wear for her wedding. It has a short, fitted sleeveless dress and a long jacket with Chinese-style buttons and short sleeves. Felshman, who's 5 feet, 10 inches and wears a size 10, ordered the outfit four days ago.

Hong Kong has a long-standing reputation as a shopper's paradise, although it is no longer the trove of bargains that it once was. But its innumerable clothing stores come up short for those who are even slightly tall or otherwise built beyond typically tiny Cantonese proportions. "I can't find my size in many Hong Kong stores, and even if I do, it doesn't fit my upper body," Felshman says.

Fortunately, Hong Kong tailors' reputation for quickly crafting quality garments is

as long-standing as its merchants'. While men's wear is the mainstay, many in areas frequented by tourists or expatriates—such as Central on Hong Kong Island and Tsim Sha Tsui in Kowloon—cater to both sexes, and some do women's tailoring exclusively.

Danny Chen, manager of Irene Fashions, which specializes in business attire for executive women, explains the appeal of custom-tailored clothes: "The fit is perfect. Clients think the prices are good for the quality. And they choose their own fabric and details." Many of Chen's customers have paid \$1,000 for a suit by Armani or Donna Karan.

But Armani's colors might not suit them, or someone else at a meeting might be wearing the same Donna Karan suit. A tailor such as Chen or Wong charges \$500 to \$700, depending on the fabric, for a suit comparable to a \$1,000 designer version. A good wool skirt might run \$100, a simple dress in the neighborhood of \$150 to \$200, and a silk cocktail dress perhaps \$300 and up.

Felshman's wedding suit came to \$425. A friend brought Felshman to Margaret Court, where the bride-to-be combed through piles of fashion books to find the right outfit. Tailors also copy garments that customers bring in, and the most talented can transform a client's idea into a finished design. Felshman found a style she liked but wanted some alterations. No problem, said Wong, who took thorough measurements, made a quick sketch, designed a pattern, and got to work. "I'd probably pay about the same if I bought something similar at a store in New York," said Felshman. "But this is custom-made."

Some Hong Kong tailors rely mainly on rock-bottom prices and lightning-quick service to attract customers. One, located in Burlington House on tourist-packed Nathan Road in Kowloon, pro-

claims on a gold-lettered window sign that he is "Record Holder for the World's Fastest Made-to-Order Suit, Made in Only 10 Hours, Fifty Minutes, and 30 Seconds."

Luckily, other tailors face different priorities. On the top floors up in Burlington House is Irene Fashions, an eight-year-old women's department of W. W. Chan Sons Tailor Ltd., a tailor for 35 years. The notion of speed-tailoring lends Irene Fashions' Danny Chen. "Generally speaking, it takes four or five days to make a suit or dress," he says. (Count on at least an extra day if fabric has to be purchased somewhere else.) A lot gets packed into that time: not just two fittings, but also an initial design consultation in which Chen will do everything from recommending fabric colors to suggesting how pockets should slant to make hips appear slimmer.

**DESIGNER LINES.** Such attention to detail makes Hong Kong tailoring addictive to many women, resident visitors alike. "I'm in this it of having tailored clothes," says New Zealander Patricia Nelson, 45. During 15 years of living in Hong Kong, Nelson has amassed a wardrobe full of business suits, evening jackets, and other apparel from Margaret Court. She got hooked when she realized she could get fashions similar to those turned out by designers—but in more practical fabrics, with a feathering style modification at fair prices.

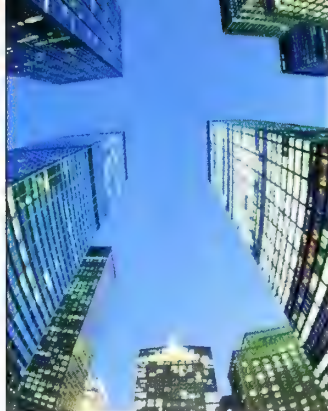
Even the best Hong Kong tailors face pressure from a growing number and quality of local retail clothing stores and rising costs owing to the colony's soaring rents. But once converted, their tastes rarely stray. And ones keep joining the fold. Says Felshman: "Even my fiancé looks through magazines now and says, 'This is a great dress! Can you get one made?'" Lenore Mayo

## Where to Have Clothes Custom-Made in Hong Kong

**IRENE FASHIONS** A2, 2nd Floor, Burlington House, 94 Nathan Road, Tsim Sha Tsui, Kowloon; 852 2367-5588, 2366-2634; serene, genteel, polite

**LUSAN MANDONGUS** 1/F, 127 Wing Lok Street, Sheung Wan; 852 2815-4592, 2542-4007; orange door, opera music wafting through the shop

**MARGARET COURT TAILORESS CO.** Room 201, Golden House, 28 Pottinger Street, Central; 852 2525-5596; bustling, informal, staffed entirely by women



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Transmedia cardholders may also apply their savings toward the purchase of airline tickets. Nor-

Fifteen-year-old In Good Taste (IGT) began expanding well before Transmedia and offers deals on flowers, boat charters, limousine rentals, hair styling, and even parking in New York City garages. Most recently, it has added discounts at hotels, such as the Marriott Orlando in Florida, and clothing stores in Mi-



of advertisements from local restaurants. These books, which cost \$30 to \$40, must be repurchased annually. And the Entertainment card discount is valid only once at each restaurant.

**GOLD CARD.** Accepted by some 70,000 merchants nationwide (Transmedia has more than 6,000; IGT, 5,000), the Entertainment card has the widest range of offerings—from cruise discounts to reduced-rate symphony concerts to cheap fast food. Cardholders present both the card and the coupon to get discounts.

The program offers a new feature this year, called Entertainment Gold, available free in all markets except Manhattan and Dallas, where it costs extra. It's similar to Transmedia and IGT in that discounts are credited to Visa, MasterCard, or Discover cards, and members can enjoy repeated discounts at participating restaurants. The savings: 25% for the first visit, but only 10% on subsequent visits.

There are downsides to discount cards, of course. Offerings vary widely from city to city. And turnover is high, as establishments become more popular and don't require discounts to lure business. Still, whether for dining or other services, the savings can really be quite tasty.

*David Swafford*

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DATA: BUSINESS WEEK

Entertainment Publications' dining card—have dropped out from restaurant into lodging, phone, even dry cleaning concert tickets. The savings typically run 20% to 30%, though sometimes even higher. "It's all about competition," said Richard Elias, an Entertainment Publications manager. Three other players, Entertainment Premier card, Dining Card (available in Illinois, Minnesota, and the West), and South Florida, are still sticking to restaurants.

Transmedia has been the one of the majors to cut its offerings. This year the company added how much as Georgetown

ally, members who dine in participating restaurants receive a 25% discount in the form of a credit on a designated Visa, MasterCard, or Discover Card. But by choosing the travel option, the savings accrue in a special account called Transmedia Dollars—and instead of receiving a 25% rebate on the restaurant tab, it's 30%. The catch is that you have to buy the ticket, then send proof of purchase to Transmedia. The company reimburses you from your travel account. If you should fail to renew your Transmedia membership while you're enrolled in the travel program, the company will charge you \$15 and send you a check for only 50% of your accrued savings.

ami, New York, and Los Angeles, says Richard Roth, chairman of IGT Services.

Unlike Transmedia and IGT, Entertainment Publications has no membership fees. Instead, it distributes its cards inside thick books

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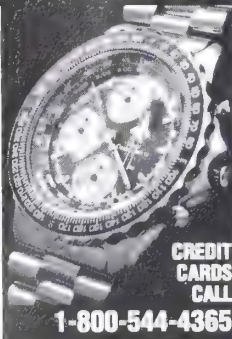
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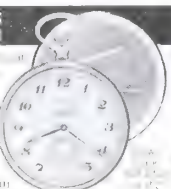


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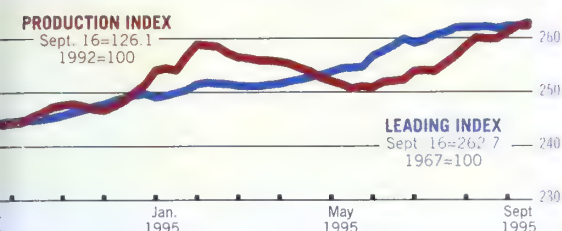
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## PRODUCTION AND LEADING INDEXES

Change from last week: 0.0%  
Change from last year: 8.7%

Change from last week: 0.2%  
Change from last year: 7.7%



The production index was unchanged in the week ended Sept. 16. Before the week of the four-week moving average, the index fell to 124.8, from 125.1, after a seasonally adjusted output of paper, paperboard, coal, and crude-oil led the decline.

The leading index was up in the latest week. The unaveraged index increased to 264.1, from 262.1 in the previous week. That gain reflected higher gains in real-estate loans.

Source: U.S. Commerce Dept. Copyright 1995 by The McGraw-Hill Companies. BW leading index copyright 1995 by CIBCIR.

## FINANCIAL INDICATORS

|                                          | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|------------------------------------------|-------------|------------|--------------|
| <b>PRICES</b> (9/23) S&P 500             | 583.69      | 579.23     | 26.0         |
| <b>BOND YIELD, Aaa</b> (9/23)            | 7.31%       | 7.29%      | -13.1        |
| <b>COMMODITY MATERIALS PRICES</b> (9/23) | 112.8       | 113.0      | NA*          |
| <b>INSURANCE FAILURES</b> (9/15)         | 307         | 384r       | 9.3          |
| <b>STATE BONDS</b> (9/13) billions       | \$499.3     | \$496.2r   | 12.2         |
| <b>SUPPLY, M2</b> (9/11) billions        | \$3,712.4   | \$3,713.2r | 3.8          |
| <b>CLAIMS, UNEMPLOYMENT</b> (9/9) thous. | 364         | 342r       | 11.3         |

\*Center for International Business Cycle Research (CIBCIR), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of companies), Federal Reserve, Labor Dept. CIBCIR seasonally adjusts data on failures and real estate loans. \*Historical data available from CIBCIR.

## INTEREST RATES

|                                        | LATEST WEEK | WEEK AGO | YEAR AGO |
|----------------------------------------|-------------|----------|----------|
| <b>MUTUAL FUNDS</b> (9/26)             | 5.73%       | 5.73%    | 4.66%    |
| <b>GOVERNMENT BOND</b> (9/27) 3-month  | 5.76        | 5.69     | 5.17     |
| <b>SAVINGS DEPOSITS</b> (9/27) 3-month | 5.78        | 5.69     | 5.21     |
| <b>MORTGAGE</b> (9/22) 30-year         | 7.82        | 7.81     | 8.89     |
| <b>CABLE MORTGAGE</b> (9/22) one-year  | 5.80        | 5.90     | 5.71     |
| <b>LIBOR</b> (9/27)                    | 8.75        | 8.75     | 7.75     |

Source: Federal Reserve, HSH Associates, Reuters Holdings PLC

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### FINANCIAL INCOME

**Oct. 2, 8:30 a.m.** ▶ Personal income likely grew by 0.1% in August, according to the median forecast of economists surveyed by MMS International, one of the McGraw-Hill Companies. Consumer spending probably rose a larger 0.5%, led by motor-vehicle sales. Incomes rose and spending was up 0.2% in July.

### SURVEY

**Oct. 2, 10 a.m.** ▶ The National Association of Purchasing Management's index stood at 50% in September, up from 46.9% level in August. The reading would imply that the factory is just treading water.

### CONSTRUCTION SPENDING

**Monday, Oct. 2, 10 a.m.** ▶ Building outlays probably increased a solid 0.5% in August. That's suggested by healthy housing activity and a rebound in nonresidential projects. Spending jumped 2% in July.

### LEADING INDICATORS

**Wednesday, Oct. 4, 8:30 a.m.** ▶ The government's composite index of leading indicators likely rose 0.1% in August, after falling 0.2% in July, says the MMS survey.

### FACTORY INVENTORIES

**Wednesday, Oct. 4, 10 a.m.** ▶ Manufacturing inventories probably increased by 0.4% in August, after leaping 0.6% in July. The

August rise is suggested by the month's 1% gain in factory output.

### EMPLOYMENT

**Friday, Oct. 6, 8:30 a.m.** ▶ Nonfarm payrolls in September grew by 160,000 slots, according to the median MMS forecast. Almost 250,000 jobs were created in August. Factories likely added 10,000 new workers in September, on top of the 12,000 hired in August. The unemployment rate probably remained at 5.6% last month.

### INSTALLMENT CREDIT

**Friday, Oct. 6** ▶ Consumers probably added \$10 billion in new credit in August, on top of \$8.8 billion taken on in July.

## PRODUCTION INDICATORS

|                                                       | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|-------------------------------------------------------|-------------|-----------|--------------|
| <b>STEEL</b> (9/23) thous. of net tons                | 1,955       | 1,965#    | 5.6          |
| <b>AUTOS</b> (9/23) units                             | 129,789     | 125,124r# | -7.5         |
| <b>TRUCKS</b> (9/23) units                            | 114,755     | 125,301r# | 0.4          |
| <b>ELECTRIC POWER</b> (9/23) millions of kilowatt-hrs | 61,631      | 64,211#   | 3.7          |
| <b>CRUDE-OIL REFINING</b> (9/23) thous. of bbl./day   | 14,298      | 14,529#   | 1.9          |
| <b>COAL</b> (9/16) thous. of net tons                 | 20,842#     | 19,849r   | 4.3          |
| <b>PAPERBOARD</b> (9/16) thous. of tons               | 865.5#      | 826.1r    | -5.9         |
| <b>PAPER</b> (9/16) thous. of tons                    | 839.0#      | 845.0r    | 1.8          |
| <b>LUMBER</b> (9/16) millions of ft.                  | 475.1#      | 389.9     | -5.1         |
| <b>RAIL FREIGHT</b> (9/16) billions of ton-miles      | 25.6#       | 23.2      | 5.3          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA<sup>1</sup>, SFPA<sup>2</sup>, Association of American Railroads

## PRICES

|                                                            | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|------------------------------------------------------------|-------------|----------|--------------|
| <b>GOLD</b> (9/27) \$/troy oz.                             | 383.750     | 384.500  | -2.9         |
| <b>STEEL SCRAP</b> (9/26) #1 heavy, \$/ton                 | 143.50      | 143.50   | 6.7          |
| <b>COPPER</b> (9/22) ¢/lb.                                 | 135.6       | 133.5    | 6.5          |
| <b>ALUMINUM</b> (9/22) ¢/lb.                               | 82.0        | 82.0     | 3.8          |
| <b>COTTON</b> (9/22) strict low middling 1-1/16 in., ¢/lb. | 92.53       | 90.04    | 31.1         |
| <b>OIL</b> (9/26) \$/bbl.                                  | 17.33       | 19.00    | -2.1         |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                                         | LATEST WEEK | WEEK AGO | YEAR AGO |
|-----------------------------------------|-------------|----------|----------|
| <b>JAPANESE YEN</b> (9/27)              | 100.15      | 103.34   | 98.48    |
| <b>GERMAN MARK</b> (9/27)               | 1.43        | 1.47     | 1.55     |
| <b>BRITISH POUND</b> (9/27)             | 1.57        | 1.55     | 1.58     |
| <b>FRENCH FRANC</b> (9/27)              | 4.92        | 5.07     | 5.28     |
| <b>ITALIAN LIRA</b> (9/27)              | 1605.5      | 1617.3   | 1556.1   |
| <b>CANADIAN DOLLAR</b> (9/27)           | 1.35        | 1.36     | 1.34     |
| <b>MEXICAN PESO</b> (9/27) <sup>3</sup> | 6.395       | 6.300    | 3.413    |

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars



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17. Signature and Title of Editor, Publisher, Business Manager or Owner

Gary M. Singer, Controller

9/18/95

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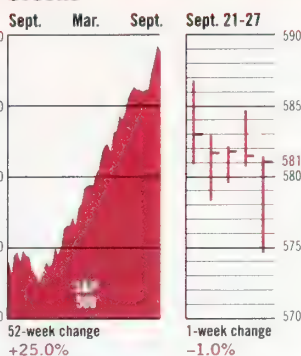
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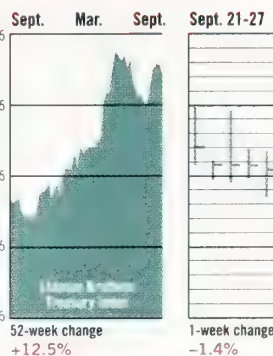
# Investment Figures of the Week

**STOCKS**  
 fell a bit this week, as  
 hit some of the tech is-  
 specific Stock Exchange  
 index, which measures  
 price of the top 100 tech-  
 stocks, fell 4.9% from its  
 Sept. 20. However, the  
 edged off the decision by  
 reserve's open market  
 Sept. 27 to leave  
 unchanged. Few invest-  
 ing a cut in rates, in  
 strong numbers on dur-  
 goods and home sales.  
 stocks tumbled in the wake  
 of the peso.

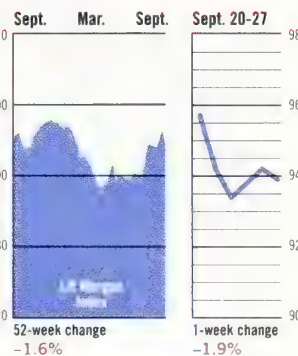
## STOCKS



## BONDS



## THE DOLLAR



## ANALYSIS

|                                         | Latest   | % change<br>Week          | % change<br>52-week |
|-----------------------------------------|----------|---------------------------|---------------------|
| <b>INDUSTRIALS</b>                      | 4762.4   | -0.6                      | 22.8                |
| <b>COMPANIES (S&amp;P MidCap Index)</b> | 213.2    | -2.4                      | 22.2                |
| <b>COMPANIES (Russell 2000)</b>         | 305.9    | -2.8                      | 20.2                |
| <b>COMPANIES (Russell 3000)</b>         | 333.7    | -1.3                      | 24.8                |
| <b>TECH STOCKS</b>                      |          | % change (local currency) |                     |
|                                         | Latest   | Week                      | 52-week             |
| <b>FINANCIAL TIMES 100</b>              | 3485.0   | -2.1                      | 14.7                |
| <b>NIKKEI INDEX</b>                     | 18,262.4 | 0.4                       | -6.4                |
| <b>DOW JONES COMPOSITE</b>              | 4500.1   | -1.1                      | 2.9                 |

## FUNDAMENTALS

|                                         | Latest | Week ago | Year ago |
|-----------------------------------------|--------|----------|----------|
| <b>90-DAY TREASURY BILL YIELD</b>       | 5.41%  | 5.33%    | 4.60%    |
| <b>30-YEAR TREASURY BOND YIELD</b>      | 6.58%  | 6.47%    | 7.81%    |
| <b>S&amp;P 500 DIVIDEND YIELD</b>       | 2.34%  | 2.32%    | 2.74%    |
| <b>S&amp;P 500 PRICE/EARNINGS RATIO</b> | 16.8   | 16.9     | 18.3     |

## TECHNICAL INDICATORS

|                                                  | Latest | Week ago | Reading  |
|--------------------------------------------------|--------|----------|----------|
| <b>S&amp;P 500 200-day moving average</b>        | 518.4  | 515.1    | Positive |
| <b>Stocks above 200-day moving average</b>       | 74.0%  | 77.0%    | Negative |
| <b>Speculative sentiment: Put/call ratio</b>     | 0.62   | 0.60 r   | Neutral  |
| <b>Insider sentiment: Vickers sell/buy ratio</b> | 2.69   | 2.54     | Negative |

BLOOMBERG FINANCIAL MARKETS

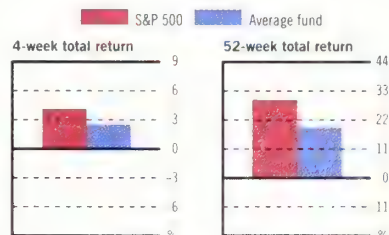
## GROUPS

|                           |  | % change<br>1-month | % change<br>12-month | Strongest stock in group      | % change<br>1-month | % change<br>12-month | Price  |
|---------------------------|--|---------------------|----------------------|-------------------------------|---------------------|----------------------|--------|
| <b>TELECOMMUNICATIONS</b> |  | 15.5                | 84.6                 | <b>TEKTRONIX</b>              | 27.5                | 51.6                 | 58     |
| <b>TELECOMMUNICATIONS</b> |  | 14.8                | 13.6                 | <b>AT&amp;T</b>               | 16.8                | 18.2                 | 64 1/4 |
| <b>TELECOMMUNICATIONS</b> |  | 12.4                | 49.4                 | <b>MCDONALD'S</b>             | 13.4                | 54.7                 | 41 3/8 |
| <b>TELECOMMUNICATIONS</b> |  | 12.3                | 58.0                 | <b>ELI LILLY</b>              | 14.9                | 58.6                 | 89 5/8 |
| <b>TELECOMMUNICATIONS</b> |  | 12.2                | 41.4                 | <b>WALGREEN</b>               | 15.8                | 46.2                 | 27 1/2 |
| <b>TELECOMMUNICATIONS</b> |  | % change            | % change             | <b>Weakest stock in group</b> | % change            | % change             | Price  |
| <b>TELECOMMUNICATIONS</b> |  | 1-month             | 12-month             | <b>CROWN CORK &amp; SEAL</b>  | -17.2               | -2.3                 | 37 3/8 |
| <b>TELECOMMUNICATIONS</b> |  | -15.6               | 0.6                  | <b>ALCOA</b>                  | -13.2               | 19.5                 | 51     |
| <b>TELECOMMUNICATIONS</b> |  | -11.5               | 15.1                 | <b>DELTA AIR LINES</b>        | -14.7               | 47.4                 | 66 1/8 |
| <b>TELECOMMUNICATIONS</b> |  | -8.0                | 29.3                 | <b>CATERPILLAR</b>            | -10.8               | 8.4                  | 58     |
| <b>TELECOMMUNICATIONS</b> |  | -7.6                | 9.1                  | <b>ROADWAY SERVICES</b>       | -9.2                | -17.8                | 49 1/2 |
| <b>TELECOMMUNICATIONS</b> |  | -7.3                | -11.5                |                               |                     |                      |        |

MORNINGSTAR INC.

## FUNDS

|                                            | %    | <b>LAGGARDS</b> |                                             | %     |
|--------------------------------------------|------|-----------------|---------------------------------------------|-------|
| <b>Four-week total return</b>              |      |                 | <b>Four-week total return</b>               |       |
| <b>EV MARATHON GREATER INDIA</b>           | 10.4 |                 | <b>FIDELITY SELECT INDUSTRIAL MATERIALS</b> | -6.8  |
| <b>PIONEER INDIA B</b>                     | 8.3  |                 | <b>PIONEER INDIA B</b>                      | -6.0  |
| <b>PIONEER INDIA B</b>                     | 8.2  |                 | <b>PIONEER INDIA B</b>                      | -4.5  |
| <b>52-week total return</b>                |      |                 | <b>52-week total return</b>                 |       |
| <b>WRIGHT EQUIFUND-MEXICO</b>              | 98.2 |                 | <b>WRIGHT EQUIFUND-MEXICO</b>               | -50.7 |
| <b>BT INVESTMENT LATIN AMERICAN EQUITY</b> | 96.8 |                 | <b>BT INVESTMENT LATIN AMERICAN EQUITY</b>  | -40.3 |
| <b>HERCULES LATIN AMERICAN VALUE</b>       | 90.2 |                 | <b>HERCULES LATIN AMERICAN VALUE</b>        | -38.4 |



## PORTFOLIOS

represent the  
 of \$10,000  
 year ago  
 portfolio  
 indicate  
 al returns

**U.S. stocks**  
**\$12,849**  
 -0.48%

**Treasury bonds**  
**\$12,390**  
 -0.95%

**Foreign stocks**  
**\$11,207**  
 +0.50%

**Money market fund**  
**\$10,543**  
 +0.12%

**Gold**  
**\$9,841**  
 -0.42%

page are as of market close Wednesday, Sept. 27, 1995, unless otherwise in-  
 dicated. Country groups include S&P 500 companies only; performance and share prices are

as of market close Sept. 26. Mutual fund returns are as of Sept. 22. Relative portfolios are val-  
 ued as of Sept. 26. A more detailed explanation of this page is available on request. r=revised



# SIGN A CONTRACT FOR GROWTH

**I**t is time to take the BUSINESS WEEK pledge. There's a Contract With America, a Contract With Virginia, even a Contract With New York, and they all promise one thing—to cut, chop, streamline, and otherwise reduce government, taxes, regulation, etc. We have another idea. How about policymakers taking a pledge to expand—the economy, that is.

We want government officials, both elected and appointed, to sign a Contract For Growth. Pledge to get the economy growing at a 3.5% annual rate, instead of the anemic 2.5% of recent years. With a bigger economic pie, balancing the budget becomes easier, wages rise, jobs multiply, you name it.

But how can the economy grow at this higher rate without igniting inflation? That's the question Federal Reserve officials, economists, and politicians have been asking for decades. Their answer? It can't. If the economy grows at 3.5%, they argue, demand soon exceeds capacity, which inevitably causes inflation. Their solution, then, is to cap growth at 2.5%—and government policy, under Republicans and Democrats alike, has been to settle for exactly that. Be satisfied, they say.

Not good enough, we say. This week's Cover Story, "Productivity to the rescue," shows why faster growth is not only possible, it's preferable (page 114). It shows why policymakers should heed the words of the National Association of Manufacturers, the folks who make things in America, which recently declared that its members can sustain a 3% to 3.5% growth rate without inflation, but can't because of the stranglehold of Washington policy.

Below the radar screen of archaic government statistics, U.S. productivity has been soaring. In the 1990s, nonfarm productivity has been rising twice as fast as in the previous 20 years (as fast as in the 1960s, when the U.S. had a 3.8% growth rate). It's not that the U.S. is just doing better—it's doing better against its competitors. The U.S. is now both the

low-cost producer and high-tech leader among all industrial nations. For the third year in a row, the Swiss International Institute for Management Development ranked the U.S. No. 1 in global competitiveness.

So why the gloom and doom? The *mal de mille ans* represented by James Goldsmith's *The Trap* and Paul Kennedy's *The Rise and Fall of the Great Powers* echoes the pessimism of past writers who didn't get it. They focus on wage stagnation and rising inequality. Yet historically, wage gains have tracked productivity gains extremely closely, but the two don't march in lockstep. There's no reason about this phenomenon. It takes that long for people to learn to use the new generation of tools and raise their value to their employers. That's what is going on today.

Bottom line, the capacity is there to support higher economic growth. Yet fearful policymakers, perhaps unwilling to buy into a grim limits-to-growth paradigm. What can be done? Congress and the White House should adopt a interim report of the congressional commission headed by Michael Boskin of Stanford University that calls for changing the Consumer Price Index, the nation's measure of inflation. The commission says the current CPI overstates inflation by a third. Dropping the CPI to 2% from 3% would bring the country's official inflation rate into line with reality. It would also show that current real interest rates are way too high.

After the CPI is changed, the Fed should lower rates sharply. A forthcoming deal to balance the budget will give the Fed cause to lower rates to compensate for the end to the fiscal stimulus that comes with deficit spending. But the Fed should go further and let the economy grow. The productivity surge gives America the capacity to grow 3.5% annually without serious inflation. Policymakers need to believe in the nation's producers and stop being so frightened.

# DEFAULT ON THE DEBT? BE SERIOUS

**'W**hen I was a child, I spake as a child, I understood as a child, I thought as a child, I reasoned as a child; but when I became a man, I gave up childish ways...."  
—I Corinthians

Washington politicians would do well to take a moment to ponder this passage. Childish bipartisan bickering has led to talk of the U.S. government defaulting on its national debt, an unimaginable act of weakness. What kind of country walks away from its obligations, and what kind of leadership advocates this kind of behavior?

In a speech before the Public Securities Assn., House Speaker Newt Gingrich said that in his negotiations with President Clinton over balancing the budget, he would be willing to let Congress stall on raising the federal debt limit and cause the government to default. His words set off a

tremor in international markets, shaking the dollar. Moves with the global bond markets these days is riskier than Mother Nature, especially for a nation so addicted to borrowing.

Sure, the Speaker quickly backed off, and yes, there are measures that Treasury Secretary Robert E. Rubin might take to fudge a default. There's the Exchange Stabilization Fund that was used to lend money to Mexico last year. In a real pinch, the U.S. could even sell part of its gold reserves. But no sensible official should even contemplate such a default. A default could mean a permanent premium in the interest rate paid by the U.S. to foreigners, even if it helps protect a peace pact on the balanced budget.

If politicians have to bluff and bluster like kids when their work done, they should do it without jeopardizing the financial health of the country. Better yet, they should grow



## The tallest recycling story ever told.

Suffice it to say, anything that's 2,232 steps to the top (in lieu of taking one of 104 elevators) is not your average office building.

Everything about Sears Tower is mind boggling. Like enough plumbing (25,000 miles) to go around the world. And enough telephone cable to encircle it  $1\frac{1}{4}$  times.

It's sort of the Mount Everest of recycling challenges. So hopefully you'll have some idea of what it took to conceive a recycling program that now covers some 10,000 people working for sixty different tenants on over 100 floors.

You certainly won't have to use your imagination to appreciate the results. This year alone 1,200 tons of paper will be collected for recycling. An amount that, if baled and stacked, would be three times higher than the world's tallest building itself.

It could be just as surprising to find out what recycling could do for your business. Please call us at 1-800-977-6272. You'll find we don't mind challenges.

*What business do we have saying we help the environment? That is our business.*



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The background of the image features several broad, expressive brushstrokes in shades of brown, tan, and orange, creating a textured, painterly effect. The strokes are layered and vary in intensity, with some appearing more saturated than others.

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shoes that  
never need  
polishing.**

SS WEEK  
October 16

# BusinessWeek



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“What Bankers Trust can do for Sony and IBM is get in the middle and rip them off.”

“Funny business, you know? Lure people into that calm and then just totally f--- 'em.”

# THE BANKERS TRUST TAPES

Here's the positive side: I buried my parents so much that it's going to take me four years to trade them out of this mess.”

In just-released court documents, Procter & Gamble brings racketeering charges against Bankers Trust.

The key evidence: 6,500 taped recording;

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# Informix's Phil White on AT&T WorldMark Servers.

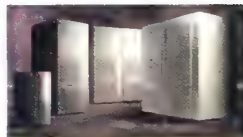
**“We** make the most scalable database in the world.  
No platform scales us better than AT&T.”

*Phil White, CEO, Informix Software*





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## BusinessWeek

OCTOBER 16, 1995

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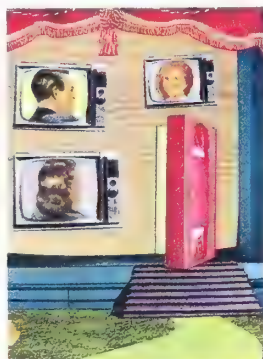
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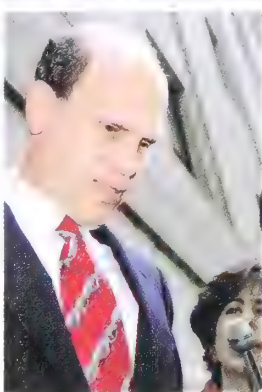
# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

## THE FEDS

### WE MEET AGAIN, MR. MILKEN

THE LUCRATIVE work done by Michael Milken on Time Warner's buyout of Turner Broadcasting System has gotten the attention of an old nemesis. The Securities & Exchange Commission is looking into whether the consulting arrangement violates a 1991 lifetime ban of Milken from securities work, says a source close to the inquiry.



UP FROM JUNK: Milken

king, who during his reign in the 1980s masterminded the financing of Turner, is receiving as much as \$50 million from Turner for his Time Warner role, according to *The Wall Street Journal*. The SEC is considering whether Milken served as an "investment adviser," which would violate the SEC's order.

But there's no clear definition of an adviser. So the SEC

**TALK SHOW** "The high criminal court has [determined] these standards give the certainty of a fair trial by the Singaporean court." —Prosecutor Hans-Hermann Eckert, after German court let Singapore extradite ex-Barings trader Nick Leeson

will try to determine exactly what kind of advice on the proposed \$7.5 billion deal merited such a hefty paycheck. The source says the SEC also wants to be careful to avoid the appearance of a witch-hunt. "Milken does have the right to make a living," the source says. A Turner spokeswoman would say only that Milken has been advising the company on "long-term strategic issues." Denying any violation, a Milken spokesman says: "The SEC did not bar Michael Milken from having ideas and vision."

Milken spent two years in prison and paid a \$1.1 billion fine after pleading guilty to felony securities-law violations in 1990. If the SEC finds that Milken has violated its order, he could be hit with contempt charges. *Michael Schroeder*

## HONCHOS

### NICE PLUG, WARREN BUT WRONG AIRLINE

WARREN BUFFETT HASN'T his investment in USAir kept him from doing ads for a competitor, Midwest Express. The two airlines go toe-to-toe on the Washington-Omaha route. But the recent *Nation's Business* campaign features a photo of Buffett in front of a West plane and quotes him praising the carrier as "the best value, though Buffett doesn't mention USAir by name, he is in the ad that Midwest Express is the only one who could be nonstop" et from Omaha to the national capital.



BUFFETT:

Nonstop fan

Midwest direct. Buffett, through an aide, says he appeared in the ad because Midwest's Omaha link is a boon to the Nebraskan economy. Both carriers charge \$468 for a seven-day advance round-trip ticket. Buffett travels to Washington regularly to keep tabs on his investments in two companies based there, *Washington Post* and, USAir.

Buffett has said the investment in USAir by Berkshire Hathaway holding company was a mistake. Berkshire took a \$268.5 million write-down on the investment this year, but a potential takeover by another airline (page 38) could let him recoup some of that. Buffett shrugs off the Buffett saying the two carriers share many overlapping routes. *Mark Le*

## LEGAL TENDER

### FOR NOW, THE GREENBACK LIVES



ONE SMALL promise in the Republican Contract With America—replacing the dollar bill with a dollar coin—is proving to be about as popular on Capitol Hill as the government's disastrous 1977 Susan B. Anthony coin goof. The idea appears doomed, as polls show tradition-bound Americans strongly against jettisoning the 130-year-old greenback for a newfangled gold-colored coin.

GOP budget-balancers had figured they could save \$112 million over five years by closing the dollar presses, which replace the entire stock of bills every 17 months. Coins, obviously, are a lot more durable. Supported by mining and vending-machine interests, proponents argued that coins minted this year

would last into the 2020s. But foes, including Clinton Administration officials, argued that smart cards, not dollar coins, are the currency of the future.

Facing certain defeat, coin supporters recently decided not to force showdown votes

in the congressional banking committees. Nonetheless, at a committee meeting, Senator Rod Grams (R-Minn.), the coin's Senate pointman, predicted eventual victory, saying: "We're on the 25-yard line, ready to score." Said Banking Committee Chairman Alfonse D'Amato (R-N.Y.): "You're on the 25-yard line—your own." *Richard S. Dunham*

## THE LIST TAKE A HIKE

Conventional wisdom says tax hikes are political suicide, especially in Newt Gingrich's Washington. But plenty of entrepreneurs are willing to pay higher taxes, if

they go to the right places. Top pick: deficit-reduction.

Here are the percentages of entrepreneurs who would strongly support tax hikes for certain initiatives:

1040

### WHERE TAX INCREASES ARE PALATABLE

|                         |     |                       |     |
|-------------------------|-----|-----------------------|-----|
| REDUCE THE DEFICIT      | 40% | REDUCE FOREIGN DEBT   | 17% |
| REDUCE CRIME            | 30% | INFRASTRUCTURE        | 17% |
| IMPROVE EDUCATION       | 29% | PRIMARY BUSINESS R&D  | 17% |
| ACCELERATE WAR ON DRUGS | 20% | ENVIRONMENTAL CLEANUP | 12% |
| CREATE JOBS             | 20% | UNIVERSAL HEALTH CARE | 10% |

DATA: ERNST & YOUNG SURVEY OF 460 BUSINESS LEADERS

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# Up Front

## BUG ZAPPERS

### NO BELFRY? HOW ABOUT A BAT CONDO?

THE HOUSING MARKET FOR bats is flying high. This has nothing to do with *Batman Forever*. Bats are suddenly popular because people now realize the winged ones consume huge amounts of bugs. A single brown bat eats 600 insects per hour.

So bat-house builders are doing a good business throughout skeeter country, from the wetlands of East Texas to the bogs of Maine. Demand for the houses,

which range from microwave-size bat-chelor pads to multichambered abodes as big as refrigerators, has expanded tenfold since 1990 at Coveside Conservation Products in Gay, Maine. The dwellings have made their way to Nature Co., Brookstone, and Wal-Mart outlets. Houston's Vida Products, which makes 1,000 bat houses a day, charges \$29.95 for a 15-bat domicile and \$89.95 for a 100-bat one.

The bat-house boom is strongest in Mineral Wells, Tex., where a conservation-minded entrepreneur has sold them to dozens of downtown businesses. Organic farmers in California's walnut groves are using bats as a sort of

## RANK AND FILE

### FROM RUNWAY TO PICKET LINE

PICTURE IT: FASHION MODELS marching in a picket line. Yes, in an industry where top names can make up to \$10,000 a day for a mega-event, a movement to organize is afoot. Why? Far below the Cindy Crawford and Claudia Schiffer models working for as little as \$60 a day. Many fall victim to fly-by-night agencies who cheat them out of wages and sleazy photographers who charge big bucks for portfolio shots

that look about as professional as something their kid brother could have taken with a disposable.

Young models "are desperate for help," says Ami Bongay, a former model who in July chartered the Model's Guild, a branch of the 13.3-million member Office & Professional Employees International Union. The Model's Guild, which claims 500 people want to sign up, hasn't officially organized anyone or

## DRAWN & QUARTERED



nontoxic insecticide. Last year, Motorola spent \$10,000 to house 5,000 of the flexible fliers around its Austin (Tex.) plant to keep bugs from annoying employees. Says structural engineer Gwen Turner: "We owe bats here a favor." *Adele Conover*

## GUERRILLA MARKETING

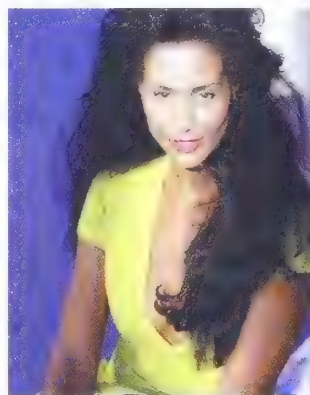
### CHE GUEVARA, CAPITALIST TOOL

CHE GUEVARA, THE sworn enemy of capitalism helped launch the Cuban revolution, is now, well, a merchandising tool.

Switzerland's Swatch, maker of some 100,000 Che watches, feeds a wave of nostalgia for when just the mention of Che—killed by the Bolivian army in 1967—packed a political wallop. Their product: a \$40 timepiece bearing Che's visage topped with a beret, and "revolución" on the band. Says Swatch spokesman Bill Schoonmaker: "It's more of a fashion style than a political statement." The watches sell well from Europe to South Florida, that anti-Castro bastion.

In London bars, you can order fruiting Che Beer. Brewed in Britain, it has citrus juices from Cuba and other Caribbean spots. Because Cuban products are used, the brew may not be sold in the U.S. *Antonio Fins*

**RADICAL?** Well, chic



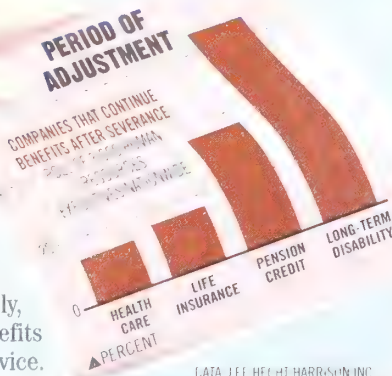
**JOHNSON:** Unionize models

started negotiations with employers yet. Famous models aren't clamoring to join. But the nascent union has gotten backing from former supermodel Beverly Johnson, who in 1974 became the first African American to grace the cover of *Vogue*.

For most, modeling is a chaotic, unregulated business. The new union, asking for dues of \$25 to \$45 per year, aims to demand such benefits as health insurance and to set industry pay standards. The union has a lot of skeptics. Says one agency executive: "The fashion industry is such a catty, fickle world. Models don't want to antagonize anyone." *Julie Tilsner*

## THE BIG PICTURE

Many downsizing victims can expect some benefits to continue for a time after they are bounced. Typically, they get a week's benefits for each year's service.







The bowerbird selects feathers, flowers and other small objects in its favorite colors to set an attractive stage for its courtship.

What could be more natural than making a concerted effort to appeal to those we'd like to win over? For the bowerbird in search of a mate, it's a simple law of nature. A law that's just as applicable when it comes to launching and marketing new products.

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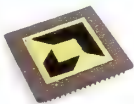
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# Readers Report

## DOES JAPAN'S FISCAL TONIC HAVE ANY KICK?

The article "Tokyo is finally grabbing the economy by the horns" (International Business, Sept. 25) overestimates the effect of recent government moves to revive the Japanese economy. The yen's current lower value is entirely artificial, and its maintenance depends in part on a quick revival in consumer spending (which would increase imports and reduce the trade deficit) in order to become permanent. The rise in the Nikkei index since its June low has had almost nothing to do with the Sept. 8 rate cut and a lot to do with foreign investment in the market. Foreigners are in effect propping up Japan's financial system.

Aside from the discount rate cut, the Ministry of Finance's moves to resolve the banking crisis are pathetically weak, and the projected solution to the housing-loan corporation crisis has been pushed back to December at the earliest. On the deregulation front, precious little has actually been done. If there is even a modest turnaround, it is likely that the process will grind to a halt.

Finally, the likely ascendancy of Ryutaro Hashimoto to Prime Minister signals a return to old-style Japan Inc., a world where bureaucrats work late into the night devising measures to expand exports and limit imports. It might work in the short run, but never in the long run.

John M. Tofflemire  
Tokyo

## NICE WORK IF YOU CAN GET IT

Regarding "The Prince," (Cover Story, Sept. 25), let me understand this. I'm born into a family that despotically rules a country that has what's probably the most disparate income distribution in the world. Among other trappings, my palace has 50 slaves (at least during my formative years, until that practice becomes too indecorous, given the abundance of moralizers abroad). I get my start through a law that compels foreign investors to pay "a local partner" 5% of their total investment, for no service in return. Let's also overlook any conflict in my being a member of the royal family.

So I amass a small fortune through this process, which we are careful not to call *baksheesh* or *la mordida*, as in other countries where it is less institutionalized. And the culmination is a glowing profile in BUSINESS WEEK, a few years

later, where I am likened to Warren Buffett. Where do I sign up?

C. B. Maddox  
New York

## A DANGEROUS GAME CALLED OUTSOURCING

Regarding your article "Is in-house design on the way out?" (Design, Sept. 25), many organizations, including mine, are beginning to outsource R&D to outside contractors and consultants. As you pointed out, these secondary sources often have the resources and knowhow required to generate high-quality products in shorter time frames.

Although it's a short-term benefit, organizations need to weigh this against the potential long-term consequences of having the understanding of important technologies reside outside the controlling and responsible organization. If a product change is needed as a result of a market- or quality-driven situation, the organization must respond, and the outside design resource may not be available.

Kevin L. Meyer  
Mountain View, Calif.

## RUMORS OF CRAY'S DEARTH...

In your article "Cray's feet of clay" (Developments to Watch, Sept. 25), your portrayal of "momentous changes...sweeping the supercomputer industry" noted some exciting trends but missed the point that Cray Research Inc. is driving many of these changes. For instance, Cray plans to ship a new supercomputer line with top speeds above the vaunted teraflops mark (1 trillion calculations per second) early next year, well before the competing system you mention. Advance orders for this Cray system are ahead of the pace set by Cray's current product, which in 1994 became the revenue leader in the emerging market for so-called scalable parallel systems.

More important, these systems are already being used for innovative new tasks including oil exploration, traffic

congestion planning, virtual surgery and advanced medical research.

Steve Cora  
Senior Director  
Corporate Communications  
Cray Research  
Eagan, MN

## BOEING: PORKLESS IN SEATTLE

Howard Gleckman's commentary "magic: Trimmed budget, brimful of trough" (Government, Sept. 4) leaves the impression that large U.S. corporations such as Boeing Co., receive substantial "corporate subsidies"—often at the expense of small and midsize firms—of the Export-Import Bank. We disagree.

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Ron Woculak  
President  
Boeing Commercial Airplane Group  
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IRE UNDONE

Rise and Hard Fall of Chris Whittle

H. Trimble

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# VE BY THE HYPE, E BY THE HYPE

is empire and reputation in tatters, erstwhile media magnate Christopher Whittle in October, dropped out a 1,500-word mea culpa *Knoxville News-Sentinel*. The o had salvaged a failing *Esquire* ne, whose Channel One network en advertisers a tap into school-'s brains, and who had launched lutionary Edison Project school-plan, felt he owed an apology doptive hometown. "Invention," red, "is not efficient. Efficiency after you invent ng, not before. And efits of invention far h the wastes inher- he process."

spin! What sizzle! ter claptrap! With a al flourish, the na- of Etowah, Tenn., king to obscure the t he had killed the omising Whittle nications with a tion of personal and extravagances, de-

recasts of revenue growth, and re-1980s unwillingness to operate g in his life on a pay-as-you-go Media conglomerates including arner Inc. and Philips Electron- ht into Whittle's vision and lost s of millions. In a Nixonesque Whittle told the *New Yorker* e that he was not a huckster. son: "A huckster has an intent ad."

aps that's true. But it hardly hittle less dangerous. At least a r stops the scam when he has is mark. The honest huckster— what Whittle was—is scarier. misled himself, he doesn't know stop shilling. He victimizes his and destroys himself. misguided and sometimes ap-

palling behavior is given sympathetic treatment, and ultimately made comprehensible, in Vance H. Trimble's biography of Whittle, *An Empire Undone*. Trimble, who also has written biographies of retailing revolutionary Sam M. Walton and Federal Express Corp.'s Frederick W. Smith, tells Whittle's story in a rambling, conversational style. The book has a pro-Whittle slant, no doubt due in part to Trimble's decision to let Whittle read the manuscript before publication. However wrongheaded

this viewpoint is, it allows us to see Whittle's demise not so much as a long-overdue comeuppance as the snuffing of potential.

It's easy to understand how Whittle developed his inflated self-confidence. His very first venture, a series of guides to orient college freshmen to their new locales, lost \$60,000. But Whittle and partners—recent University of Tennessee graduates all—persuaded a UT professor to keep funding them. And the guides and various spin-offs eventually earned millions. This prompted the young entrepreneur to target ever-larger game: advertisers looking to reach narrowly defined targets. For them, he developed single-advertiser magazines, wall posters, and other new media. All were heavy on advertising, light on content, and fat targets for critics of Whittle's commercialism.

In 1979, Whittle and his college buddy Phillip Moffitt shocked New York's media community by acquiring the floundering *Esquire*. By 1986, Moffitt and Whittle split up their partnership—and friendship—in a divorce that left Whittle with the publishing company and Moffitt with control of *Esquire*.

Describing this period, Trimble be-



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## Books

gins spelling out Whittle's chief flaw: inability to delegate, an almost megalomaniacal belief in his own ideas, and a huge appetite for the trapping of wealth. These observations are offered side-by-side with Trimble's odes to the entrepreneur's charm and insight. Uttered by a partner, Whittle went into creative overdrive, dreaming up ideas as the *Special Reports* single issue magazines and Channel One. Each time a project seemed to be failing, Whittle began to brainstorm spin-offs, with his plans sketched on yellow legal pads.

Over time, Whittle's investors learned to dread those legal pads. After *quire* and *Special Reports*, Whittle seemed to lose the golden touch; he continued to act like a Midas. He commissioned celebrity architects to design a Vermont vacation home and a lavish New York apartment. He bagged trophy hires, such as former Jimmy Carter aide Hank Jordan and former Yale University President Benno C. Schmidt, at poly salaries. He traveled in a corporate jet, pledged \$5.2 million to create the Whittle Scholars program at UT, and spent \$50 million on a Knoxville headquarters—"historic Whittlesburg."

The author shows us a Whittle who reached these heights just as his company was hitting its depths. The local News Network, which beamed advertising-supported educational material to doctors' offices, was a bust. The education establishment rejected Channel One as crass commercialism, and to raise cash, it was sold to the K-I investment firm. Whittle's lofty plans, Edison, his extravagance, and his failings as a manager all converged. A group of backers, led by Philips Electronics, seized control. Other investors were bailed out.

The Edison Project—Whittle's brilliant conception, which combined mandating courses with the latest technology and teaching methods—fell victim to the empire's demise. In 1985 the project was scaled down as Whittle and Schmidt sparred for control. To keep Edison afloat—and to hold out a modicum of control—Whittle sold one of his four homes. The last time *Time* interviewed him, Whittle rhapsodized about the Edison Project's outlook: "yellow legal pads already had notified for some possible spin-offs," *Time* writes. All together now, former Whittle investors: "Uh-oh."

BY DAVID GREISINGER

Atlanta bureau chief Greisinger predicted Whittle's decline.



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BY STEPHEN H. WILDSTROM

## CAN YOU BANK ON I-WAY SECURITY?

**W**hen you fire up Microsoft's Windows 95, the computer starts by demanding a password. The security looks impressive, but a computer-literate 13-year-old could get at all the files on the hard drive.

Windows NT boots up with a very similar log-in screen. But NT's protection against unauthorized access is good enough to pass stringent government security tests. How are you supposed to know what is secure and what is not?

The unfortunate answer is that you cannot. The latest reminder came when two University of California students discovered a relatively easy way to decrypt credit-card numbers and other supposedly secure messages sent out by Netscape Communications Corp.'s popular World Wide Web browser software. Netscape moved swiftly to plug the hole, and the company's high-flying stock only swooned briefly.

**"NOVICE ERROR."** I suspect, however, that the incident will have longer-lasting repercussions for the infant business of online commerce. People's willingness to engage in online transactions requires "a perception of security," says Scott Randall, general manager of NECX Direct, which sells computer hardware and software over the Internet. Today, that perception doesn't exist, and Netscape and others building online bazaars will have to work a lot harder to create both a sense—and the reality—of safety.

Knowing that security was the key to Web commerce, Netscape made the right start by licensing technology from RSA Data Security Inc., the acknowledged leader in the field. But programmers made what Purdue University security specialist Eugene Spafford calls a "novice error." One of the keys to Netscape's encryption and decoding process was the time of day of the transaction.



Figuring that out enabled someone armed with the right software to crack the code in minutes.

Netscape is hardly the only computer company to be tripped up by a security blunder. For example, Sun Microsystems Inc. once shipped workstations with microphones set up so that when the workstation was connected to the Internet, some Net surfers could listen in on office talk. And numerous software companies have spread viruses to their customers through program-distribution disks.

Netscape is determined not to repeat its errors. It made

details of the repaired Navigator available for public inspection, a step that might well have avoided the original problem. Navigator 2.0, to be shipped by yearend, incorporates both stronger encryption and a provision for digital signatures, which allow the recipient of messages to be certain that the sender is who he or she claims to be. Such "authentication" is vital to the growth of Net commerce, especially riskier forms such as online banking and business-to-business exchanges of information.

"There's no such thing as a completely safe computer or service," says Spafford. "All you can do is develop an appropriate level of trust." Developing that trust will

take hard work by software companies and Net merchants, and the comfort level will rise with experience and the passage of time. Only then will online sales climb above the low-seven-figure business it is today.

**WILY WAITERS.** A few years ago, many people were reluctant to buy from catalogs by giving out credit-card numbers over the phone. Even today, there are probably riskier places to use

your credit card than the Net: You could, for instance, hand it to a clerk or waiter who is part of a fraud ring. Either way, your liability for fraudulent use is limited by federal law to \$50.

It's perfectly reasonable, however, for consumers to be hypercautious. Personally, I'll be willing to try a few credit-card transactions after the new Netscape Navigator goes through its initial shakedown. But I'll need a lot more convincing before I'll expose my bank account to online perils. Right now, you won't be missing much if you let online commerce get started without you.

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for more comfortable typing, stereo sound, a 90-megahertz Pentium processor, and a 1-gigabyte hard drive. The lithium-ion battery gives a claim to 3 to 9 hours of use, and you can easily swap the cord for a second battery without tools. All of this weighs in at a hefty 7.4 pounds. But if you can afford the \$7,500 price tag, maybe you can hire someone to carry it for you.

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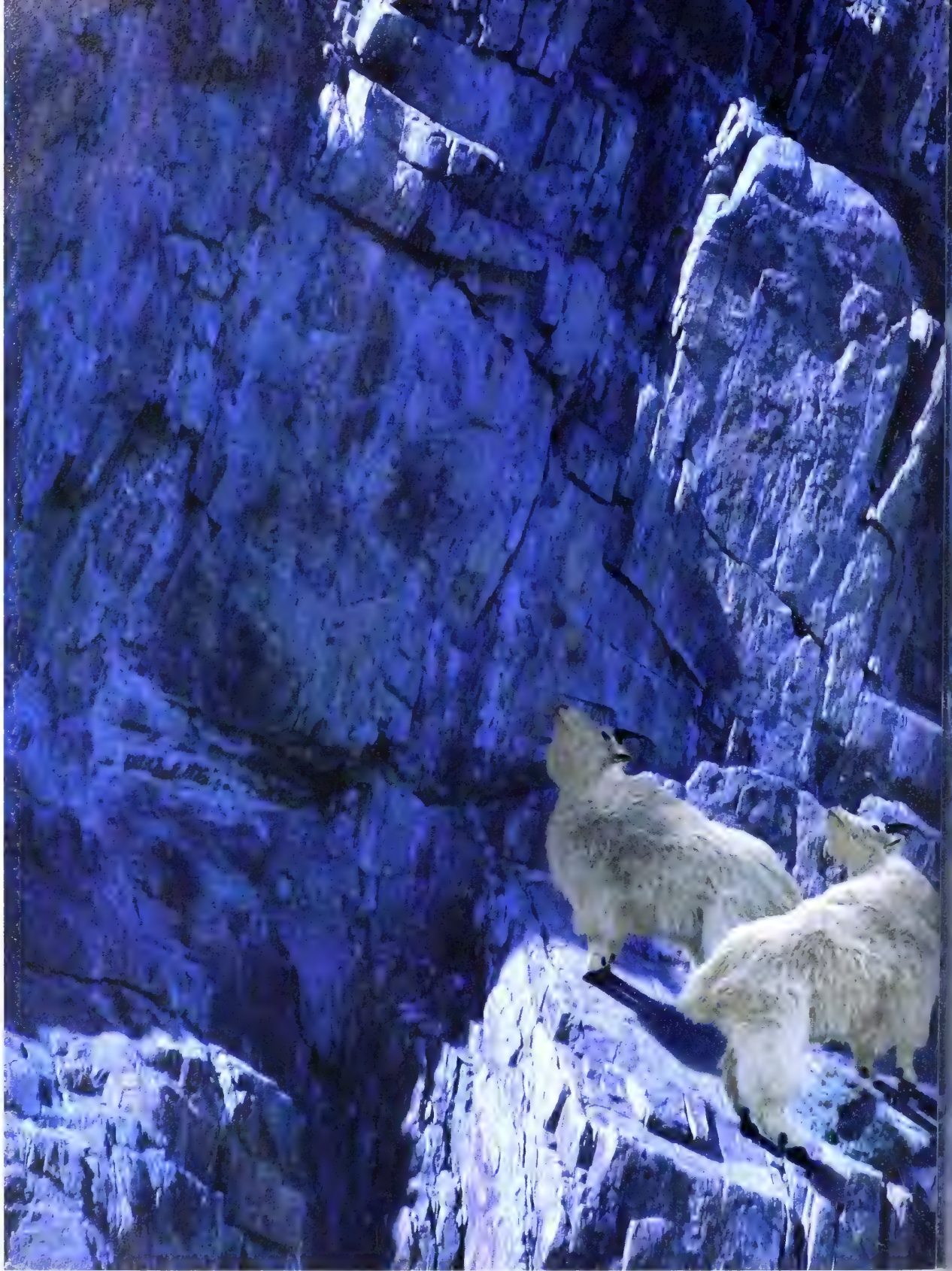
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BY GARY S. BECKER

## HOUSEWORK: THE MISSING PIECE OF THE ECONOMIC PIE



**REAL VALUE:**  
Ignoring household labor distorts growth statistics and robs those who stay at home—mostly women—of self-esteem

**H**ousehold production is an important part of the output of all nations, yet housework is not recognized when measuring the goods and services that make up the gross domestic product. This undervalues the contributions of women, since they are responsible for most of household production.

Families and other households are in effect small factories that even in the most advanced nations produce many valuable services and goods. They rear children, prepare meals, and provide shelter. They take care of sick members, give nursing and other assistance to the elderly, and perform many other helpful tasks.

Women contribute about 70% of the total time spent at these activities—even in egalitarian nations such as Sweden. They do virtually all the housework in poorer nations such as India. Some feminists argue persuasively that including housework in the GDP would raise the “consciousness” of women, especially in the less-developed world where women are badly treated. This would help to improve their bargaining position in marriage, since many housewives would “earn” more than their husbands if a woman’s household contribution had a monetary value. Yet other feminists do not want explicit calculations of production for housewives, because that would conflict with their agenda of getting women out of the household and into the labor force.

**LONG HOURS.** It is time to recognize housework as part of the goods and services in a nation’s GDP. The long hours spent at housework suggest that production in the home is a sizable percentage of the total output of all nations. After all, when a family hires someone to care for the children, clean the house, and cook, that work is counted in the GDP figures. When a parent does it, it is not.

There are several ways to quantify and measure household production. Although GDP only includes the production of goods and services that are bought and sold, they do include a value for owner-occupied housing by using the cost of rental housing that has comparable space and amenities to owned housing. The value of housework can be measured by what it would cost to buy services in the marketplace (such as baby-sitting) to replace those provided by parents.

These methods are used by Robert Eis-

ner of Northwestern University in his study *The Total Incomes System of Accounts*. Eisner finds that the imputed value of household production in the U.S. exceeded more than 20% of gross national product from mid-1940s to the early 1980s—the last year of his estimates. Much cruder calculations by the U.N. in its latest Human Development Report indicate that household production is worth more than 40% of world output.

**SWEDISH SUBSIDIES.** Neglect of household production in calculating the GDP distorts measures of economic growth. The huge increase in labor-force participation of married women during the past several decades is mainly at the expense of a reduction in the time women spent at unpaid household production. The rapid increase in GDP during these decades neglects the sizable decline in time spent on housework.

The substitution of market production for household production is clearly the reason for the rapid expansion of the child-care industry since the late 1970s. Working women reduce the time they spent caring for their own children by hiring other women to do it for them. Women cared for one another’s children.

My colleague at the University of Chicago, Sherwin Rosen, studied a situation in Sweden where the child-care industry is unusually extensive, partly because it is subsidized by the government. He does not take a stand on whether children are harmed when mothers work. However, he does show that these subsidies caused considerable inefficiencies by artificially inducing many women to enter the labor force. For example, subsidies lowered the price to women of child-care services below its true cost. I found his conclusions persuasive, but they have been controversial in Sweden because many people there want to “nationalize” the family, making government responsible for children. They want to encourage mothers to leave the labor force so that they must hire other women to care for their children.

Including housework in measures of economic growth would raise the self-respect of women who stay at home to care for children and do other housework. It would also provide a more accurate picture of GDP growth and might lead to a different interpretation of public policies that affect the allocation of time between household work and market work.

Gary S. Becker, the 1992 Nobel laureate, teaches at the University of Chicago and is a Fellow of the Hoover Institution.



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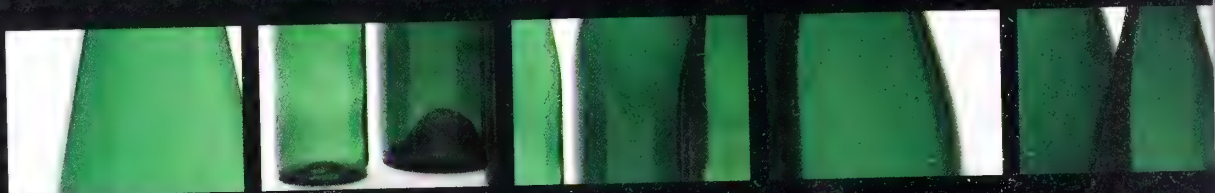




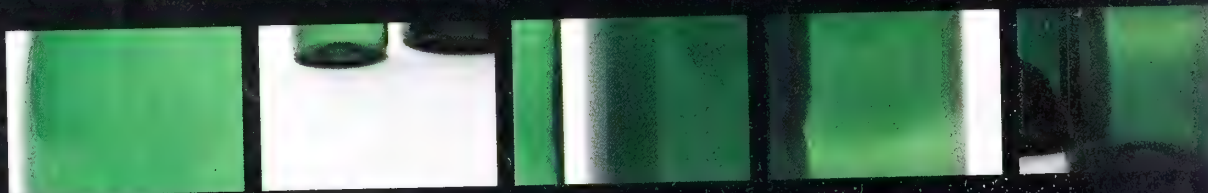
You're on the road. With a client.



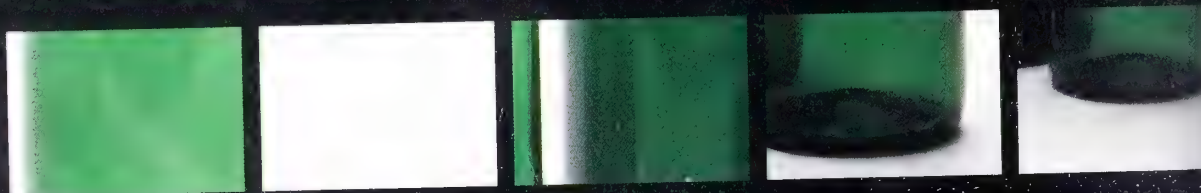
You need to locate a bottle design.



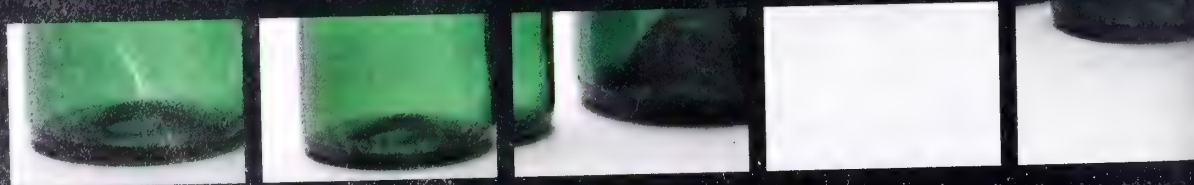
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BY CHRISTOPHER FARRELL

## EXPORTS: THESE SPOTS ARE HOT

Some regions get a bigger boost

Exports are playing an ever-larger role in the U.S. economy. What's more, they are exerting a powerful—although uneven—influence on regional growth. Last year, merchandise exports accounted for an 8.6% share of gross domestic product, up from 5.9% in 1988. But in the Pacific region, according to Steven G. Cochrane, economist at Regional Financial Associates Inc., merchandise exports as a share of gross state product (GSP) rose from 7.7% in 1988 to 12.1% in 1994. This part of the country benefited from explosive growth in the Pacific Rim countries of Asia. And in California, export growth of more than 15% last year contributed 1.5 percentage points to GSP and was a vital force behind the Golden State's economic recovery.

Similarly, the industrial Midwest is an export leader. The contribution of exports to Michigan's economic growth dou-

ly to trade with Mexico, exports boosted Texas' growth by nearly two percentage points in 1994. With the Mexican economy now in a severe recession and the peso devalued, U.S. merchandise exports to Mexico in the second quarter of 1995 were down by 15% from the fourth quarter of last year. Mexico won't generate much export activity in the Southwest this year or next.

## REINING IN U.S. HEALTH COSTS

Insurance premiums trail inflation

Good news from the health-care front. For the first time in 10 years, the rate of growth in private-sector medical care premiums fell below the rate of overall inflation and medical inflation, according to a survey by KPMG Peat Marwick. Corporate cost-containment efforts through the widespread use of managed care plans, such as health maintenance organizations and preferred provider organizations, are clearly working. In its fifth annual survey of health benefits, the firm found that corporate health plan premiums increased an average of just 2.1% so far in 1995 vs. a 3.2% rise in overall inflation and a 4.6% advance in medical inflation. The improvements in limiting premium price increases are striking. As recently as 1991, premiums jumped by 11.5%.

## WHAT RUSSIANS REALLY MAKE

They're getting more than wages

What's going on in Russia? Economists are scratching their heads over the yawning gap between income and wages in post-communist Russia. Since 1990, real wages have plunged by more than 60%, while real national income has barely budged. One reason may lie in a shift in employee compensation from wages to other types of income, says Gregory Fossedal, director of emerging markets at Lehman Bell Mueller Cannon Inc., an economic forecasting firm in Arlington, Va.

Labor income is heavily taxed in Russia, with a top income-tax rate of 62% on \$10,000 a year and 49% on \$5,000. In sharp contrast, taxes on business and property income range from 28% to 38%. Thus, companies are increasingly paying

some of their workers' salaries in stock, dividends, and other lower-taxed income, says Fossedal.

One tactic is for an employer to open a special, high-interest account in a bank for employees. The gains in these accounts are taxed at 12% to 38%, without Social Security taxes. Companies can also use these banks to arrange loans at 1% interest to employees, says Fossedal. The number of Russian commercial banks has grown from fewer than 700 at the end of 1990 to more than 3,500 today, and some of this growth is tax-related. Perhaps "bank" is becoming less of a four-letter word in Russia.



## ALL REGIONS SHARE IN WORLD TRADE

EXPORT SHARE OF GROSS STATE PRODUCT

|                    | 1988 | 1994 |
|--------------------|------|------|
| New England        | 5.0% | 7.5% |
| Middle Atlantic    | 4.5  | 6.4  |
| South Atlantic     | 4.5  | 7.2  |
| East North Central | 5.9  | 9.3  |
| East South Central | 3.6  | 6.4  |
| West North Central | 3.6  | 5.4  |
| West South Central | 9.2  | 13.0 |
| Mountain           | 3.1  | 6.0  |
| Pacific            | 7.7  | 12.1 |

DATA: REGIONAL FINANCIAL ASSOCIATES INC.

bled in 1994, as exports of autos, auto-related products, and industrial machinery boomed. In the mountain states, growth would have been 1.1 percentage points lower last year without exports. Colorado's industrial machinery and computer-equipment sales gained 50% over last year, to \$1.8 billion, for example. In the Northeast, however, the impact of exports has been just about average in recent years, says Cochrane.

Of course, being dependent on international trade can backfire, at least in the short run. Last year, West South Central states such as Texas and Louisiana received the largest regional boost from overseas sales. Thanks large-

## GONGING THE BELL CURVE

A study says it misreads key data

Those who attack *The Bell Curve* and its claim that IQ is the most important factor behind economic and social success in America are getting new ammunition. A National Bureau of Economic Research paper by Sale D. Korenman of the University of Minnesota and Christopher Winship of Harvard University reanalyzes the data behind the late Richard J. Herrnstein and Charles Murray's conclusions and throws cold water on their judgment.

The NBER study argues that *The Bell Curve's* estimates of the impact of IQ are overstated because Herrnstein and Murray rely on too narrow a measure of parental social and economic status based on education, occupation, and income only. Winship and Korenman add other important elements to the mix: background, such as whether a child grew up in a single-parent household and lived in an urban neighborhood. Their expanded measure finds a statistically bigger effect from family background on socioeconomic outcomes. Korenman and Winship go on to estimate that the effects of family background could be as much as two to four times as large as the effect of IQ. The study concludes that Native intelligence is only one of several factors determining who gets ahead.



## THE ECONOMY LOOKS POISED TO PICK UP A NOTCH

### U.S. ECONOMY

When the Commerce Dept. first reported the second quarter weak economic growth, economists said not to worry. Their argument: The mix of sturdy demand and slowdown in inventories implied good things for future growth. The way the third quarter is shaping up, you can get ready for the same spiel. Based on the third-quarter data available so far on consumer spending, construction, and personal income, and on the implications from the latest purchasing managers' report, real gross domestic product last year appears to have grown at an annual rate of 2.5%, up from 1.3% in the second quarter. The number will depend greatly on what Commerce reports for inventory growth and net foreign trade—two sectors of the economy for which there are no third-quarter monthly data available.

### OUTPUT PICKS UP AS INVENTORIES FALL



What's clear is that demand by consumers and businesses held up well. Real final sales probably advanced close to their 3.4% pace of the second quarter. Rising aftertax incomes, good job gains, and a surge in August car buying combined to lift consumer outlays. And while business investment in equipment slowed, outlays for nonresidential

construction took up some of the slack in investment. At the same time, businesses kept whittling away at excess inventories. The rebound in industrial output suggests that whatever surplus merchandise that built up was sold off by the end of September. Inventory adjustment no longer will be a significant drag on GDP growth in coming quarters. In fact, Commerce's monthly data show that manufacturing inventories held steady in August.

The mix of resilient demand and stable inventories is a positive outlook for the fourth quarter and beyond. It suggests the economy will be stronger than its 2%-or-less growth during the first three quarters of 1995.

### MOVING GROWTH PROSPECTS

These were a key reason why the Federal Reserve held rates steady at its 26 policy meeting. In fact, as far as future policy goes, the economy's health and inflation seem to have taken a back seat to the federal budget debate. It was the implication from the recently released minutes of the Fed's Aug. 22 meeting. The report said

that "consideration would need to be given to an adjustment in the committee's policy stance, especially if substantial fiscal restraint were to be enacted."

Such an overt statement might have been directed at Congress and the White House, rather than at the financial markets, the usual target of arcane Fed speak. The Fed appears to have been extending the carrot of lower rates if Washington can put together a credible package of deficit reduction.

The Fed next meets on Nov. 15, two days after the expiration of the current continuing resolution, which is temporarily funding the government. Unless a budget agreement is hammered out by then, the Fed seems likely to leave policy on hold yet again.

### IF THE LATEST DATA

were the only factor in the Fed's thinking, you could start putting away your hopes for another rate cut. They suggest that, just when the maximum impact of past rate hikes is coming to bear, the economic outlook is gradually improving.

For example, throughout this year's slowdown, consumer spending has been resilient. That has been a key factor helping businesses restore balance to their inventories. Consumer spending on goods and services, adjusted for inflation, surged 0.8% in August. Even if September outlays were flat from August, real consumer spending for the third quarter will have risen at an annual rate of 3.5% (chart).

A jump in car sales accounted for most of the August increase. Excluding motor vehicles and parts, real outlays rose only 0.2%. Car sales in September appear to have cooled off from August's 15.7-million annual pace. However, the strike at Ryder Systems Inc., the trucking company that delivers a lot of Detroit's vehicles—especially for General Motors Corp.—depressed sales.

Nonauto sales seem to have held firm in September, judging by the weekly survey of department and discount stores by Johnson Redbook Service. Through Sept. 30, the Redbook tally shows a 1.4% sales gain from August.

One reason is healthy income growth. Although personal income was flat in August, and real aftertax earnings were down slightly, strong gains in both June and July mean that third-quarter income still scored a

### SPENDING AND INCOMES LOOK STURDIER

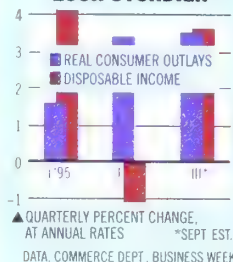


PHOTO: JEFFREY M. HARRIS FOR ENR



good gain. The bad news for retailers is that shoppers still head for the sale tables first.

For manufacturers, the pickup in consumer demand is allowing inventories to adjust more quickly, paving the way for faster production and hiring.

In fact, that shift may already be occurring, according to the September survey of the National Association of Purchasing Management. The NAPM's overall index edged up to 48.3% in September from 46.9% in August. The index is still below the 50% mark, indicating the factory sector remains lackluster.

However, the sluggishness can be traced to a big drop in the inventory index, which fell from 45.2% in August to 40.8% in September, the lowest reading in nearly four years. The NAPM said that its other indicators of factory health—output, new orders, and employment—picked up in September. A busier factory sector in September is also indicated by the BUSINESS WEEK production index. Also, the NAPM's index of prices paid fell for the eighth month in a row.

**OF COURSE, CONSUMER SPENDING** is not the sole reason to expect the economy to pick up steam. Business investment and housing also added to growth in the third quarter and should help out in coming quarters as well. Business equipment investment showed some weakness in the third quarter. But after growth rates averaging 18%, a pause is not unusual.

However, businesses are spending more on new construction. Total new outlays for building projects slipped an unexpected 0.2% in August, but that followed jumps of 0.9% in June and 1.6% in July. Even after adjustment for prices, construction staged a comeback in the summer (chart). Most of that bounce came from commercial real estate projects, especially retail space.

In addition, home buying has held up surprisingly well, given the tight stance of Fed policy, and that demand has kept homebuilding afloat. New single-family home sales fell 9.6% in August to an annual rate of 710,000. But the drop reflected a strong revision in the July sales rate from 715,000 to 785,000.

So far, the third-quarter new-home sales pace is far above the second-quarter rate. That has helped to clear out the supply of uncompleted homes—another example of inventory adjustment in the economy.

While the monthly numbers have looked a bit uneven—a key reason why the markets have rollercoastered—the summer data echo the spring. The economy may not look too exciting, but as most economists tell you, there's not much reason to worry, either.



## ARGENTINA

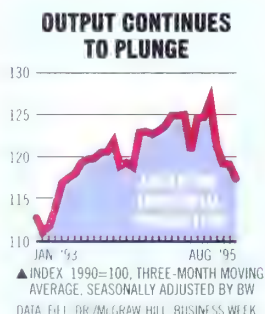
### THE PAIN MAY START TO EASE A BIT

Argentina's economy remains mired in recession, but the outlook is improving. One reason is because of waning fears that Economy Minister Domingo Cavallo, the author of the country's successful reform program, will resign amid clashes with politicians over his assertions in mid-August of corrupt practices in the policy-making process.

In late September, Cavallo traveled to the U.S. and Europe to assure investors that he is committed to working with President Carlos Menem and that the government remains dedicated to policies that encourage a sound currency and low inflation. As a result, Argentine stocks began to rally in late

September, after falling some 17% since mid-August.

The political friction arises mainly from the recession's added sting amid Cavallo's painful reforms. Argentina's real gross domestic



product fell 3.7% in the second quarter, the first decline after four years of growth averaging 7.6% per year. The recession stemmed from capital flight in fear that Argentina would devalue its currency after the Mexican peso crisis. By all

signs, the contraction continued in the third quarter. Industrial output through August remains in a steep drop (chart).

The official forecast, recently lowered, calls for 1% economic

growth in 1995 and a rebound of 5% in 1996, with inflation holding at about 3% next year. Private analysts are less upbeat about growth. They expect 1995 GDP to be flat to down a bit, with 1996 growth closer to 3%.

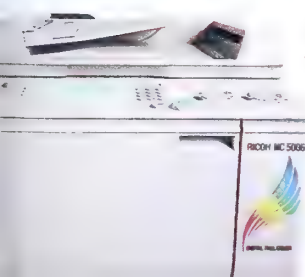
A key clash centered on splitting Cavallo's ministry, thus diluting his influence, in a bid to reverse falling production and rising joblessness, now at a record 18.6%. Menem's draft 1996 budget appears to reject such a plan. In fact, the proposed balanced budget is a vote of confidence for Cavallo. It is austere and reflects policies consistent with International Monetary Fund guidelines.

With deposits slowly returning to the banking system and foreign capital flowing in again, the foundations for recovery are gradually falling into place.



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## AIRLINES

# BIRD-HUNTING SEASON?

## A possible USAir deal may signal more consolidation

**F**or U.S. airlines, the drumbeat of retrenchment has been echoing for years. Now, with USAir Inc.'s sudden announcement on Oct. 2 that it is holding preliminary merger talks with both United Airlines and American Airlines, a new period of consolidation may be about to begin. Even the possibility that United or American may pull off a deal to buy ailing USAir could well force rivals to contemplate bulking up, too. "Once you pull that trigger, you've got all the other gunslingers out there," says Jon F. Ash, managing director of consulting firm Global Aviation Associates Ltd.

Indeed, the USAir merger talks are likely to have far-reaching ramifications. The talks could help redraw the international aviation map, if USAir partner British Airways PLC is forced to cut a new deal with another U.S. carrier. Watching its major rivals on the move, Delta Air Lines may have to consider getting into the act, especially given that a combined United-USAir or American-USAir would hold nearly 30% of U.S. domestic traffic. Ditto weaker carriers such as Continental and TWA, which is scarcely in better shape than USAir. Most of all, the talks are forcing executives to abandon their all-consuming focus on retrenchment. The big

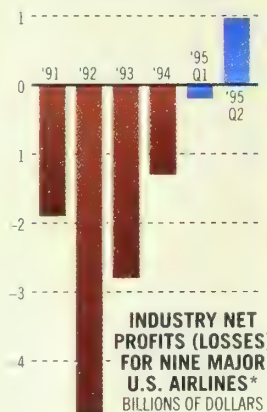
question now, says a former top airline executive: "How do you position your [carrier] with a large enough presence and market share to win in the next downturn?"

Of course, any deal is still a long shot. Antitrust issues, thorny labor problems, and financial obstacles may prove insurmountable. Many investors are hardly enthusiastic about a possible combination. The day after announcement of the talks, USAir's stock jumped, but that of UAL, parent of United, fell 3.5%, while shares in AMR, parent of American, dropped 3%.

**BIG LOSSES.** If a deal does come off, analysts see all sorts of intriguing combinations being considered in its wake. Northwest Airlines, now one of the industry's most profitable carriers, could make a nice fit with Delta or Continental, which has dramatically improved operations,

analysts say. Continental's hubs in Houston and Newark would complement Northwest's strongholds in Minneapolis, Detroit, and Memphis. And Delta could benefit from North-

### A BOUNCE-BACK IN PROFITS...



\*BEFORE EXTRAORDINARY GAINS

DATA: AIRWATCH REPORT



strong routes in the northern and the Pacific. Indeed, if a USAir isn't squelched by political or anti-concerns, "everyone will be stumbling themselves" to find their own partners, predicts one airline executive.

It itself will be pushing hard to something happen. Its motivation: survival. Although USAir finally posted losses of nearly \$3 billion in the last five years, suffered two fatal air crashes, and scuttled talks this summer to wrest \$2.5 billion in concessions from its unions. Chief Executive Seth E. Schofield, who had planned to resign, now will stay on until the merger talks are concluded.

Meanwhile, USAir's scramble to hook up with a stronger rival is already having widening reverberations.

For instance, British Air-

ways, which owns 21.5% of USAir, has been helped mightily by its three-year partnership with the U.S. carrier, despite recently having to write down half its \$400 million investment. It claims its stake in USAir has brought it \$100 million worth of benefits from sharing facilities and feeding passengers into its international routes. Without USAir, "BA's whole transatlantic network would be in jeopardy," says a former United executive.

**CACTUS DANCING.** BA itself, like other foreign carriers, is excluded under U.S. law from doing a full buyout. If United were to buy USAir, it likely would have to choose between sticking with current partner Lufthansa and switching to BA. And if American does the deed? Sources close to the carrier say it was talking with BA about an alliance before it ever contemplated a deal with USAir. But American and BA are big competitors in the transatlantic market. And then there's the possible culture clash between BA's domineering chairman, Sir Colin Marshall, and AMR Corp.'s strong-willed Robert L. Crandall. "It would be like rolling around with a cactus," says Chris

Avery, a London-based analyst with Paribas Capital Markets Group.

The pitfalls of a USAir deal may weigh heavily against the enticements. USAir's East Coast network would fill gaps for United and American and boost transatlantic traffic. But that could be more than offset by USAir's sky-high costs and intransigent labor force, says Steve Lewins, an analyst at Gruntal & Co. "I hope the stock prices come down so far so fast that the idea gets

abandoned quickly," he says. A deal also would undermine American's and United's plans to boost their below-investment-grade credit ratings by adding about \$7.9 billion of debt and leases to the acquirer's balance sheet.

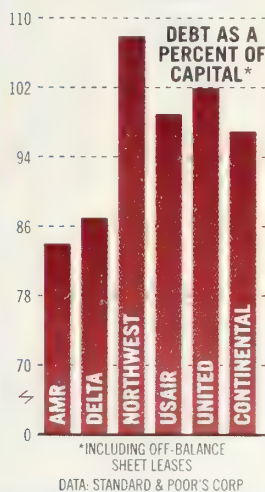
Financing problems pale compared with the labor complexities. A USAir pilot-union source points out that a merger would lead to inevitable conflicts in merging seniority lists, and he worries about possible job losses. Then there would be the effect on cost-cutting if employees get riled up. American is trying to gain \$300 million in cost savings from its pilots, and it has vowed not to invest more in the airline business until it brings costs down. United last year sold a majority stake in the carrier to its unions, after wresting \$5 billion in labor concessions. Employees there might resist any deal that dilutes their investment. "How does [a possible deal] work for us as shareholders and employees?" asks a source close to United's pilot's union. "It has to pass both tests."

Still, the pressure will be intense for some sort of USAir buyout, even if the carrier ends up being sold off in pieces. American is particularly worried about the prospect of USAir falling into United's hands. Nabbing the carrier for itself would give American coveted slots at Chicago's O'Hare, New York's LaGuardia, and Washington's National Airport. That could help American narrow the gap with United in Chicago, where it is a struggling No. 2 despite its massive hub there. Mulling a USAir deal is "a top-burner issue" at American, says a source close to the company.

The nation's two largest carriers may yet pass on doing a deal for USAir, despite their intense rivalry. But they have opened the door to a possible shakeup in an industry that lately has seemed downright staid.

*By Wendy Zellner in Dallas, with Christina Del Valle in Washington, Susan Chandler in Chicago, Paula Dwyer in London, and Stewart Toy in Paris*

### ...BUT DISMAL BALANCE SHEETS





## POLITICS

# ON A CLEAR DAY, YOU CAN SEE A BUDGET DEAL

The GOP infights are ugly, but Bill and Newt may come to terms

House Republicans attack as treason Senate Republican talk of scaling back a \$245 billion tax cut. House Speaker Newt Gingrich (R-Ga.) suffers an embarrassing setback when rebellious rookies sink a leadership-backed defense appropriations bill. And polls show that, increasingly, voters are convinced that GOP deficit-cutting plans are a radical raid on America's social safety net.

Given the turmoil, it's no surprise that the conventional wisdom increasingly says that the wheels are coming off the Republican Revolution. But while GOP troops are suffering their first real casualties in their war on the Welfare State, their balanced-budget mission remains alive and well. Indeed, even as squabbling Republicans regroup during Congress' Columbus Day recess, strategists on both ends of Pennsylvania Avenue see the emerging outlines of a budget pact that gives Republicans many of their key agenda items.

The reason: President Clinton and his GOP antagonists have significantly narrowed their policy differences, having concluded they have far more to lose from a budgetary blowup than from an 11th-hour accommodation. "When you start to piece things together, you have the makings of a deal," says a top Clinton adviser. Adds Representative James C. Greenwood (R-Pa.): "There will be a deal, and the deal will put laurels on Newt's head."

The key elements, as envisaged by the White House and Hill leaders: A balanced

budget within seven or eight years, a tax cut of about \$200 billion that would include a family tax break and a lower capital-gains rate, and Medicare savings of some \$200 billion over seven years. The package is also likely to end the federal entitlement to welfare and Medicaid, hike Pentagon spending, and soften proposed GOP cuts in such domestic programs as education and environmental protection.

Such a deal would achieve far more than Republicans dreamed possible a year ago. "If you look at the big picture, we'd really accomplish quite a bit," says Stephen Moore, director of fiscal policy studies at the libertarian Cato Institute. Still, talk of compromise has some firebrands crying sellout. "Even tough talkers Gingrich and [Senate Majority Leader Bob] Dole appear to have sunk beneath the red-ink waves without so much as a gurgle," grouches David Rucker, director of Associated Conservatives of Texas, an activist group.

Can Dole and Gingrich keep their restless troops in line? Under a temporary truce, Clinton and the GOP agreed to

keep the government running until November. If there still isn't an agreement by then, Gingrich is raising the specter of letting the government default on its debts for the first time.

It may, however, prove easier for the GOP to horse-trade with the White House than to settle nasty intra-party squabbles. Maybe it's the curse of majority status, but Republican lawmakers suddenly are beginning to look at all the world like their old Democratic rivals—carving up one another for home-state pork and ideological points. One example: a huge \$243 billion defense spending bill rejected by the House on Sept. 29. The vote followed a revolt by religious conservatives who failed to win a provision barring abortions in overseas military hospitals. They were joined by Democrats and some GOP deficit-hawks, who objected to buying more weapons than the Pentagon requested.

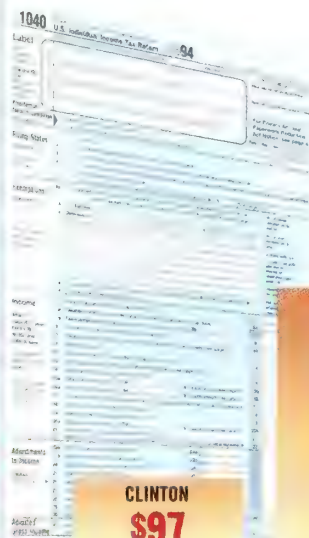
**PRIOR COMMITMENTS.** That battle does not even compare with the bitter arguing over taxes. House Republicans insist on a cut of no less than \$245 billion. Dole triggered a round of recriminations just by conceding he doesn't have sufficient Senate votes because of resistance from moderates. "We're not the uglies, and it's going to get ugly before it gets pretty," says R. Bruce Tenen, senior vice-president of the U.S. Chamber of Commerce and a key player in the deficit-slashing effort. Adds a GOP budget strategist: "The President

is sitting there fat, dumb, and happy, while we tear each other to shreds."

Behind all of this Republican discord is some not-so-subtle Presidential politics. Senator Phil Gramm (R-N.Y.) is appealing to hard-line Republicans as a compromiser. "It's the Republicans started living up to the commitments we made in the [1994] election," Gramm thunders. Dole needs to

## A Billion Here, A Billion There...

BUDGET



DATA: OFFICE OF MANAGEMENT & BUDGET, HOUSE AND SENATE BUDGET COMMITTEES





results to promote his credentials as effective leader. And Gingrich, who ruled out a '96 run, could enhance standing with the right by forcing a station with Clinton—and then by a deal more favorable to the GOP. Clinton has plenty at stake, too. By promising, he wins credit for slashing deficit while protecting seniors' harsh GOP cuts in Medicare and

Medicaid. Sighs House Republican Conference Chairman John A. Boehner (R-Ohio), "We could get 99.5% of what we want, and Clinton will declare victory."

A firm deal is not yet at hand. There's always the danger that House conservatives may desert Gingrich as a matter of principle. And the bitter Dole-Gramm rivalry could produce gridlock in the Senate. Still, the odds are that when the fi-

nal budget vote comes, Gingrich, Dole, and Clinton will conclude they have too much at stake to play a game of political chicken. It might not be the end of the welfare state, but war-weary GOP generals will have scored a big victory over government as we've known it.

*By Howard Gleckman, with Richard S. Dunham, Susan B. Garland, and Mary Beth Regan, in Washington*

## COMMENTARY

By Mike McNamee

# THE GOP HAD BETTER GET BUSINESS OFF THE DOLE, TOO

Christmas came early on K Street. Washington's business lobbyists awoke one morning in September to find a \$40 billion gift from Ways & Means Chairman Bill Archer (R-Tex.): a proposal that companies reclaim and spend massive assets locked away in overfunded pension plans. The loop-hole was designed mainly to please budget-cutting Republicans, who will garner \$10.5 billion in taxes if companies pull \$40 billion in assets, as expected. But Archer's gift was a big hit in Corporate America—and like the very best presents, it was pretty much a surprise. "We didn't ask for it," says a pension lawyer, "but you can bet we're defending it now."

Too much for ending "corporate welfare" as we know it? Early this year, Republican radicals swore they would erase the GOP's image as the Skybox Party. House Budget Chairman John R. Kasich (R-Ohio) targeted \$30 billion in special corporate tax breaks for elimination. Strategists dreamed of a public-relations disaster if Republicans slashed the social safety net while leaving a cocoon of billions in subsidies and breaks. Big Business.

**CHALLENGED.** Did the majority Republicans get the message? No. They have learned to talk the talk: Archer, for example, portrays his pension-raid plan as the centerpiece corporate tax reform." But in reality, "corporate welfare continues to be challenged," complains former aide James P. Pinkerton. Even the GOP's struggle to carve \$1 trillion off the budget over the next seven years can't shake its reflexive urge to shower business with federal lar-

gesse. If they can't repress that instinct, Republicans will never convince voters that they have been reborn as the champions of the middle class.

Most of the biggest corporate breaks were never in peril. Oil drillers and timber companies didn't lose

fare, lobbyists have come roaring back. Iowa Republicans reminded House Speaker Newt Gingrich (R-Ga.) that they're hosting the first event of the 1996 primary season—and persuaded him to eliminate the Ways & Means panel's cap on tax breaks for ethanol, a boon to corn farmers and agribusiness giant Archer-Daniels-Midland Co. Home-state shipping interests prevailed over ideological purity for Senate Majority Whip Trent Lott (R-Miss.), who forced \$46 million in maritime subsidies back into the budget. Budget pressures ultimately may doom some subsidies. The imperative to cut \$13 billion from farm programs, for example, may guarantee that something like the Freedom to Farm Act—a 7-year reduction in price supports—will prevail. The pork that's packed into the Pentagon's appropriation will certainly be trimmed

in hard negotiations between Capitol Hill and the White House. And tax breaks for pharmaceutical makers' Puerto Rican plants, long under assault, may slowly wither away.

That's a start—but it's not enough. A GOP that believes social welfare breeds personal dependency can't go on pretending that corporate welfare builds a strong economy. The party that's bold enough to reform health care for the elderly ought to show the same fortitude when tackling oil drillers and airplane manufacturers. If Republicans can't wake up to the glaring disparity in their positions, they can be sure the voters will.



any sleep over their loopholes—not with Texan Archer and, until recently, Oregon Senator Bob Packwood in charge of tax policy. Republicans who had long denounced the "socialism" of the Tennessee Valley and Bonneville Power authorities "got real quiet when their party started winning seats in the Northwest, the land of cheap electricity," says Robert J. Shapiro of the Progressive Policy Institute, a Democratic think tank. Big exporters will continue to enjoy sales help from the Export-Import Bank and the Agriculture Dept.'s marketing-promotion programs.

Even where budget-cutters did propose small nicks in corporate wel-

*McNamee covers economic policy.*



## CONGRESS

### WHY THE TELECOM BILL IS IN SLO-MO

AT&T allies and Bell backers are in a shootout on the Hill

Edward K. Christian isn't the type of executive to leap blindly into a business deal. Since July, the CEO of Detroit-based Saga Communications Inc. has been shopping for more radio stations to add to the 25 he already owns. He was banking on congressional passage this year of an overhaul of the nation's communications laws—reforms that would lift limits on the number of stations one company can own. But suddenly, Christian has put his deals on hold. "I can't make business decisions based on maybes," he says.

It's the Pause that Retrenches. While final passage this year looked like a sure bet only last month, the biggest overhaul of telecommunications legislation in 60 years has hit speed bumps on Capitol Hill. Now, it's possible that reforms won't be enacted until next year, a casualty of the traditional end-of-session crunch in Congress.

What has gone wrong? Representative John D. Dingell (D-Mich.), a supporter, says that with lawmakers struggling to pass a balanced budget, tax cuts, and welfare overhaul, the telecommunications bill "is running into inexplicable delays."

**COMPROMISE?** Actually, the delays are not so inexplicable. Behind the scenes, a battle royal rages. In August, long-distance companies were dealt a big setback when the House passed a version of the bill that would let the Bells get into their business fairly easily. Since then, supporters of the long-distance companies have staged a rearguard action to soften the legislation. Even Speaker Newt Gingrich, normally a strong Bell backer, hasn't done much to fight off the long-distance forces.

There also is growing unease among

Democratic lawmakers that deregulation—even the prospect of it—will help create overpowering communications giants. Case in point: Time Warner Inc.'s proposed \$8 billion acquisition of Turner Broadcasting System Inc.

The House and Senate bills differ in a

### The Fight Isn't Over

*Telecom reform looked like a sure thing this summer. But work has since slowed to a crawl. How industry stands on the legislation.*

#### PRO



RAYMOND SMITH



JOHN MALONE

Local-phone company chiefs such as Bell Atlantic's Ray Smith want quick action. Reform would let them offer long-distance service once phone regulators certify that their local markets are open to competition. TCI's John Malone and other cable leaders like rapid cable deregulation.

#### CON



ROBERT ALLEN



BERT ROBERTS

AT&T's Bob Allen, MCI's Bert Roberts, and other long-distance executives are gleeful about the delay. They want a higher hurdle in place before the Bells can enter long-distance markets: certification by the Justice Dept., not just phone regulators, that their local markets are competitive.

few key respects: The House version not only gives local phone companies a break, it also favors cable-television interests. The Senate version goes easier on long-distance companies. Creation of a joint conference panel to hammer out those differences in a compromise measure is way behind schedule. Gingrich spokesman Tony Blankley says that his boss still hopes to pass a bill this year.

Telecom reform continues to draw broad bipartisan support on Capitol Hill. But a delay gives more time for regrouping by the White House—which has threatened a veto over cable deregulation, media concentration, and the

terms under which the Bells can get into long distance. Other bill opponents include several major consumer organizations. The longer passage takes, the more leverage critics will have to extract concessions. "Time is on our side," says Bradley Stillman, a telecommunication expert for the Consumer Federation of America.

**HEADACHE.** The long-distance coalition taking advantage of the extra time cast the House bill as a consumer nightmare. The measure would let the Bells into the long-distance market before their local markets are open to competition, the group charges. "It let the local phone companies pick a

pocket," one new opposition leader declares. Broadcasters are pressing to remove a provision that would allow for installation of a "violence" filter in new TVs that would allow parents to block objectionable broadcasts. Vice-President Al Gore

using every chance he gets to argue that cable rates can skyrocket should they be deregulated.

With the process in slo-mo, GOP concessions may not follow. The bills for removal of cable rate regulation in early 1997. But Democrats are betting they will be able to delay the effective date long enough for cable competition to develop. "We think we can get it pushed back," says Larry Irving, a telecommunications adviser for the White House. And there might be some new

restrictions on media concentration, as well. Right now, the House and Senate measures call for removal of a federal rule that bars one company from owning the newspaper, cable, TV, and radio stations in any given community. But Congress is now expected to pass at least part of the anti-monopoly provision in conference.

Delays are a headache for CEOs like Christian who want to get on with their dealmaking. In its broad outline, telecom reform legislation is still intact. But the bill that finally emerges from Congress—when it emerges—will be more of a compromise than the measures passed so far.

By Mark Lewyn in Washington

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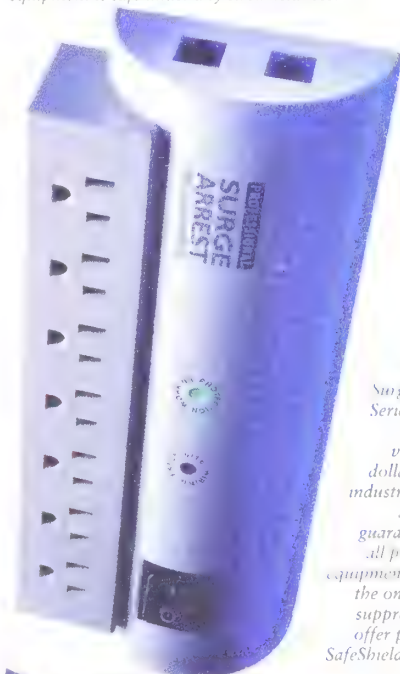
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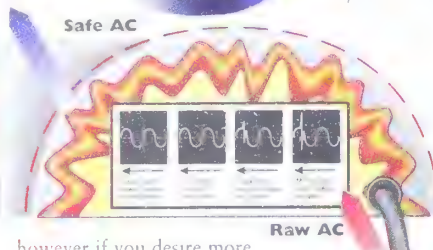
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STRUCTURING

# APPLE KICK THE MESSENGER?

Graziano's exit may mean continuing business as usual

Head has rolled at Apple Computer Inc.—but was it the right one? Despite wild rumors the board would oust Chief Executive Michael H. Spindler at its Oct. 3 meeting, it instead renewed support for Spindler and accepted the resignation of long-time Chief Financial Officer Joseph A. Graziano. Apple cites simple “differences of opinion” between Graziano and Spindler.

The move may be simple, inside the company, but they are fundamental: whether to sell off a part of Apple, as Graziano insisted, or continue business as usual. Internal critics of Spindler's leadership say that Apple, by shrinking market share, operational gaffes, the onslaught of Windows 95, can't afford the status quo anymore. “I have liked to see far more,” says CS First Boston analyst J. William Gurley.

## DIVORCE

Spindler seems to have little interest in pursuing a merger

It's time for someone to be accountable. Apple's stock fell 1%, to 36%, on the day its lowest price in nearly a year. **“RAY.”** Spindler, who declined to comment, has said in recent interviews the current strategy is fine. Others disagree. “The place is in total disarray,” says one former executive, who adds that the company is rapidly separating into pro-Spindler and pro-Graziano camps.

Now that Graziano—who some say is the best-qualified person to replace Spindler—is gone, others say the shake-up isn't over. Company watchers say that L. Eilers, the powerful head of consulting, is firmly in the Graziano camp. Meanwhile, the rank-and-file is abiding over edicts to cut expenses in the face of an profits shortfall. Wall Street figures fourth-quarter earnings are in at little better than \$70

million, vs. \$114 million a year ago.

The problem: Having underforecast demand, the company has a \$1 billion-plus order backlog that leaves it unable to take advantage of booming PC demand. Worse, it has made little progress in its attempt to spawn a clone market by licensing out its MacOS software. Only three small licensees are shipping product. And no major player is expected to



## GONER

Graziano figures the numbers are going the wrong way

that barring an “indecent proposal” from a suitor, “there's no strategic fit that makes sense.” Says one associate: “The Macintosh is a religion to Mike, and he wants to see it sustained.”

But nowadays Apple may need more vision and less religion. Problem is, Graziano may have taken much of that vision with him. The 52-year-old, CFO from 1981 to 1985, was lured back from Sun Microsystems Inc. in 1989 with a \$1.5 million signing bonus.

He was known as a team player who could still make tough calls. “He was the rudder and the voice of reason,” says former Apple software chief Yogen K. Dalal, now a Mayfield Fund partner.

Spindler's future may not be quite so certain either. Markkula, who dominates

Apple's board, says he supports Spindler. But “when your chairman comes out and says he has complete confidence in you, then it's time to worry,” says co-founder Steven P. Jobs, who was ousted in 1985. The turmoil at Apple probably hasn't run its course.

By Peter Burrows and Kathy Rebello in Phoenix, with Robert D. Hof in San Francisco

get on board until late next year, when a new architecture for computers that can run both Mac and Windows software is released. Even if that works, it's hardly a windfall, in that Apple would be trading sales of \$2,500 machines for \$45 licensing fees, says Dataquest Inc. analyst Kimball Brown.

Graziano knew that didn't add up, Brown says. “He knows the numbers, and he knows they're not going the right way.” The only alternative: to merge with a company with the marketing and financial clout to help Apple survive the switch to a software-based company. The most likely candidate, many think, is IBM Corp.,

## WORRIED SHAREHOLDERS





LABOR

# RYDER'S ROCKY ROAD TO THE BARGAINING TABLE

Going it alone against the Teamsters has been a costly mistake

**W**hen Ryder System Inc. and other car-haul companies sat down to negotiate a new labor pact early this year, Ryder was determined not to give in to the Teamsters again. In their last go-round with labor, in 1992, the trucking companies had agreed to limit the growth of nonunion subsidiaries. This time, Ryder planned to stand firm against such demands. As the largest hauler, with a third of the market for new-car transports, Miami-based Ryder figured it was better-positioned than rivals to withstand a strike.

Ryder badly miscalculated. It tacitly admitted as much on Oct. 3, when the company agreed in secret talks with the Teamsters to ease its hard line on the use of nonunion labor. That freed up the union and the industry to resume talks on Oct. 5. "There have been discussions that have brought down some of the barriers to negotiations," confirms Steven C. Nichols, a senior vice-president of Ryder's car-haul unit. The two sides should have a new pact soon, insiders say.

**UP THE JUNCTION.** Why is Ryder backing down now? The Teamsters waited to strike until after the slack summer season for car sales. And when the union moved on Sept. 7, it moved only on Ryder. The result: While rivals have continued to ship cars to dealers' lots, Ryder's car-haul unit will lose \$10 million pretax in the third quarter, the company estimates, vs. a \$9.6 million profit during the same period last year.

Ryder's largest customers were hit, too. The strike was part of the reason General Motors Corp.'s September auto sales showed only a disappointing 0.3% increase over a year earlier. Chrysler

Corp.'s sales plunged by 6.6%. "We're losing sales because we don't have product," fumes Ken Hubble, general manager for Herb Chambers Dodge in Danvers, Mass. Lack of inventory has cut his autumn sales by \$100,000, he says. Meanwhile, his dealership still is being invoiced for cars stuck at the railhead.

Ryder's main mistake was in thinking it could quickly and easily ride out a

felt they could not reach an agreement with Ryder," on this issue, says R. Hunter, the chief negotiator for the industry bargaining association. Says Teamsters negotiator Doug Weber "Ryder overreached."

Ryder tried to hold its tough stance after the strike began. It sued the union in federal court and sought an injunction by the National Labor Relations Board. The agency, however, rebuffed Ryder's claim that the strike was illegal. The lawsuit, which contends Ryder is losing \$1 million a day in revenues to the strike is still pending. Ryder didn't anticipate such losses, which will slice third-quarter earnings by some 15%, to about \$35 million, says Gruntal & Co. analyst Steven Lewins. "When [the strike] started, we were hopeful that it could be resolved



**PICKET FENCES:** STRIKERS BLOCK A DODGE CONVOY IN WARREN, MICH.

The strike badly hurt the auto industry. "We're losing sales because we don't have product," says one dealer

strike. Many of the 16 other car haulers whose labor pacts expired on May 21 have been trying to undercut the Teamsters' \$17-an-hour average wage with new, often nonunion units. However the other carriers were less aggressive about shifting business to such units than Ryder. Because car hauling comprises only 14% of its \$4.6 billion in sales, Ryder figured it had more financial clout to withstand a strike. It also knew that the union had to borrow \$15 million to get through a 1994 freight strike and had cut weekly payments to strikers to \$55, from \$200.

So when the other car haulers were ready to give in to the Teamsters, Ryder balked. "We were very close and the Teamsters exited the talks because they

within a week and wouldn't have made an impact," says Ryder Chief Financial Officer Edwin A. Huston.

Meanwhile, pressure has been growing from the car companies. GM ships about 60% of its cars and trucks to Ryder, while Chrysler ships some 40% (Ford uses Ryder for less than 1%). GM will have to close plants if the strike continues much longer, says Burnham Securities auto analyst David Healy.

Ryder may yet emerge from the strike with more freedom to use nonunion labor than its rivals. But it will take a lot of explaining to convince shareholders that it was all worth it.

*By Gail DeGeorge in Miami  
Aaron Bernstein in New York,  
Keith Naughton in Detroit*



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SCANDALS

## UNDER THE BORDER, DOWN MEXICO WAY

Were L.A.'s Reynoso brothers importing more than food?

**O**n the surface, it was the American dream come alive. In just 15 years, José Reynoso and two of his brothers, Antonio and Jesús, built up a hugely successful business importing food from Mexico. Their \$37 million, Los Angeles County-based Reynoso Brothers Food Corp. and four other importing companies made the elder José, 63, the very embodiment of the immigrant success story: He lived in a 13,000-square-foot mansion, was a prominent figure in the Latino community, and was featured recently in a Los Angeles television show on immigrants. Too bad the story may now turn out to be a hoax.

Along with canned chilies, spices, and tomatoes from Mexico, the Reynoso brothers were importing tons of cocaine, according to a Sept. 28 federal indictment filed in San Diego. It alleges that the brothers were the linchpin in a cocaine-smuggling and money-laundering scheme orchestrated by Mexican drug lord Joaquín "Chappo" Guzmán.

The most damning charge: that an un-

finished 1,416-foot-long, 65-foot-deep, air-conditioned tunnel under the U.S.-Mexican border was to be used as a cocaine pipeline running directly into a Reynoso cannery facility within the U.S. near San Diego. There, investigators charge, trucks were to load cans of cocaine concealed as food products for distribution across the country. There was just one hitch: Prosecutors say the Reynosos relied on inaccurate San Diego County maps to construct the tunnel. So instead of leading to the warehouse, the tunnel dead-ended about 100 feet short of it.

**"AIR OF LEGITIMACY."** José Reynoso has pleaded not guilty. "There hasn't been one gram of cocaine found at his house or place of business," says his lawyer, James E. Blancarte. "They've taken a man with a long and well-established reputation and destroyed it." Meanwhile, his brothers are said to be holed up in Mexico. The tunnel was discovered in 1993 but never linked to the Reynosos until now. Though it never carried drugs, the feds allege that the Reynoso family and others were able to ship

**TOOT SUITE:** The narco tunnel ended in the open desert on the U.S. side.

more than eight tons of cocaine from 1991 through 1993 via their food distribution network stretching from the San Diego border to Chicago, New York, and elsewhere. The indictment suggests that Guzmán, now serving a jail sentence in Mexico in connection with the 1993 murder of the Roman Catholic cardinal of Guadalajara, Juan Jesús Posada Ocampo, hired the Reynoso brothers in 1991 to "lend an air of legitimacy" to the organization's shipments of Colombian coke.

Key to the smugglers' success, say prosecutors, was Antonio Reynoso's ingenuity in concealment. In one case, wiretaps led authorities to cocaine-filled plastic tubs that were submerged in railroad container cars filled with soybean oil. A bust in Tecate, Mexico, in 1993 found more than seven tons of cocaine concealed in cans of La Comarca brand jalapeño chili peppers.

All that would have paled beside an operation that was allegedly being run in the U.S. The indictment contains a detailed allegation of how José and Jesús Reynoso spent \$2.1 million to build a warehouse and cannery on a tract of land near the border. The crowning achievement was to have been the subterranean link to Mexico, dubbed by authorities the "narco tunnel."

The Reynoso indictments come as a blow to Los Angeles's 3.3 million Latinos. Not only does the company employ hundreds of immigrants, but the family is known for its support of Latino scholarships. "As far as we know, this was a good, strong, family-owned business," says Steven Soto, president of the Los Angeles-based Mexican American Grocers Assn.

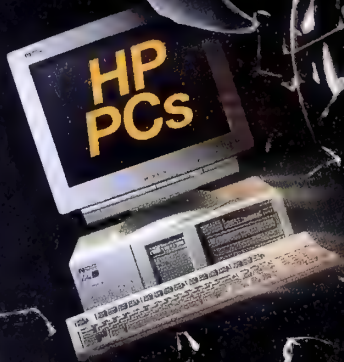
Well, not quite. The family already has had its share of trouble. In 1972, José Reynoso's son, Rene Cruz, was extradited to the U.S. after he fled south of the border to avoid murder charges. He was later convicted of slaying the owner of Los Angeles' Central Wholesale Market.

For now, the family business continues to operate. But if the U.S. Attorney's office proves its case, the Reynoso brothers' American dream is over, dead-ended in a 65-foot-deep tunnel to nowhere.

By Eric Schine in Los Angeles

From the tunnel, feds say, trucks were to be loaded with cocaine disguised as food for nationwide distribution





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B-SCHOOLS

## A TRADE WARRIOR GOES TO YALE

Jeff Garten will need all his diplomatic skills at the B-school

**J**effrey E. Garten is no tweedy academic. As Commerce Under Secretary for International Trade in the Clinton Administration, he was a point man in fractious auto trade talks with the Japanese. He also provoked outrage among American trading partners by aggressively helping U.S. companies gain big contracts overseas. Now, he's quitting his government job to take over as dean of Yale University's School of Management. When he reports for work on Nov. 1, the 48-year-old former investment banker will probably need every wily diplomatic skill at his command.

Yale's B-School is still trying to live down the controversial legacy of airline exec Michael E. Levine, who as dean from 1989 to 1991 managed to anger students and alumni by gutting the organizational-behavior and operations-research faculty. The school traditionally has trained leaders for government and nonprofit organizations, as well as corporations; alumni charged that Levine wanted to narrow its mission and turn it into an MBA factory.

Things got pretty hairy during the Levine years. Students showed up at graduation wearing black armbands, and alumni rented flyover

planes that unfurled anti-Levine banners. Alumni support waned, and applications fell. To help polish its external image, Yale even hired the public-relations manager who helped Union Carbide Corp. through its Bhopal disaster. "It was a period when many of us had a hard time either contributing to the school or recommending it to others,"

says Michela English, a 1979 alumna who is now a senior vice-president of the National Geographic Society Inc. Though he is not a Yale, Garten



### JEFFREY E. GARTEN

**BORN** Oct. 29, 1946, in New York City

**EDUCATION** BA (1968) from Dartmouth College, MA (1972) and PhD (1980) from Johns Hopkins

**CAREER** As a Commerce Under Secretary, this former investment banker focused on export growth in emerging markets

**FAMILY** Married for 26 years to Ina, who runs Barefoot Contessa, a gourmet food shop in East Hampton, N.Y.; no children

### HITTING THE BOOKS IN NEW HAVEN

*Applications, and hopes, are way*

has devoted himself to a career has mixed both public and private vice. Throughout his 15 years as an investment banker, he has made numerous detours, serving in the Nixon, Ford, Carter, and Clinton Administrations.

His international experience is vast, too. After earning a master's degree in international affairs from Johns Hopkins in 1972, he got a job in Henry Kissinger's State Dept. In 1978, he joined Lehman Brothers Kuhn Loeb, where he specialized in restructuring Latin American debt. As a managing director of Shearson Lehman Brothers from 1984 to 1987, he opened and ran up the firm's Tokyo office.

**A CHARMER.** Garten's two-year stint as Commerce Under Secretary saw him emerge as the architect of a strategy to expand U.S. exports into key emerging markets such as China and India. He also won plaudits for creating an "economic war room" where executive government officials could plot strategy to win billion-dollar deals overseas.

That brought him to the attention of Yale University President Richard Levin, who began wooing Garten in early June. Garten says he accepted the job partly because being in Washington had forced him to spend too much time apart from his wife, Ina, who owns a gourmet food store in East Hampton, N.Y. Married for 26 years, they met when he was a freshman at Dartmouth and she, then 16, was visiting her brother there.

In Washington, Garten is known as a charmer, an adept public speaker, and a bit of a publicity hound. All are qualities that may serve him well in continuing the Yale management school's turnaround. Applications hit 1,427 this year up from 1,107 in 1991, and the average Graduate Management Admission Test (GMAT) score was a record 664 for the newest enrolled class, up 22 points in two years. "We are no longer perceived as an embarrassment to the university," says Professor Stanley J. Garstka, who served as acting dean.

Garten's mission now: to keep the improvements coming while loudly trumpeting the school's increased performance. "I want to give it the same luster in the field of management as Yale has in law," he says. Garten doesn't yet have specific plans for doing that. But once he gets going, Garten has been shot at making a deep imprint on a long-troubled institution.

*By John A. Byrne in New York*





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## BASEBALL

## THE BOZOS OF OCTOBER

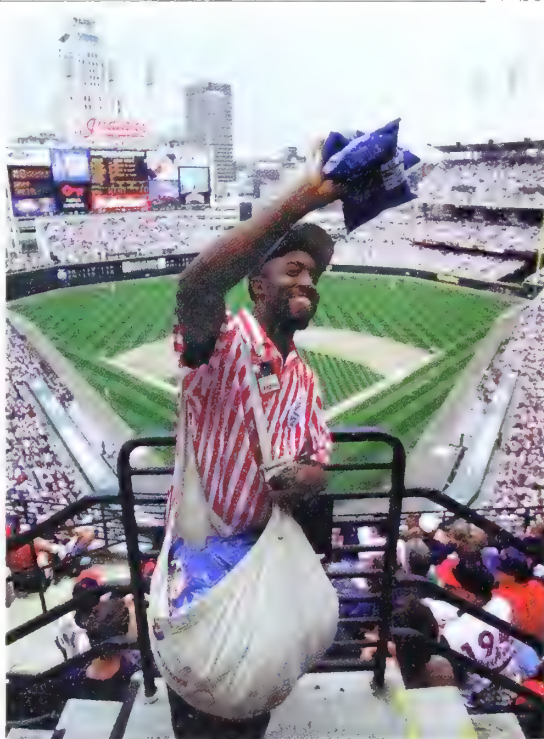
It's a tough job, but the owners are making fans even angrier

In 1986, the year the Boston Red Sox played the New York Mets in the World Series, Boston native Larry Swasey was in a New York hospital with a serious heart condition. His doctors playfully told Swasey his allegiance to the BoSox might adversely affect their treatment program. This year, Swasey is sick again—sick to his stomach. The Red Sox are in the playoffs, but he can't get a game on TV. Because baseball is experimenting with its first regionalized playoff broadcasts, he'll get only the hated New York Yankees games at home. "I'm very, very upset with baseball," Swasey moans.

Join the crowd. Just when baseball fever should be hitting its peak with the launch of the classic fall playoff series, the mood is lousy. Regional playoff broadcasts are just the latest insult to fans who saw the players' strike snuff last year's exciting pennant drive and the World Series. Meanwhile, baseball is still plagued by all its old problems: labor strife, cash-strapped teams, a commissioner vacancy, and a failed broadcast strategy.

Irate fans and the lack of progress are costing baseball plenty. League insiders estimate that leaguewide revenues will reach just \$1.4 billion this year, well below the \$1.8 billion in 1993. Attendance started the season down 20% from last year and didn't budge, despite the new "wild card" format designed to boost late-season numbers. National broadcasting revenues will come in 20% below 1993's \$1 billion, while local broadcast and cable advertising will fall to \$400 million, a 30% drop. The numbers are so bad that even millionaire ballplayers are taking a hit. Average pay dropped to \$1.07 million from \$1.26 million, the first decline in eight years.

**MUTUAL SUFFERING.** That spells trouble in ball yards nationwide. Franchises that appreciated at a 15% annual rate prestrike are stuck in neutral: The Oakland Athletics, which projected a \$20 million loss this year, sold for only \$85 million. And newspaper heir Kevin McClatchy wants to pay the same



amount for the near-dead Pittsburgh Pirates, also spilling \$20 million in red ink this year. "We need to have a new order of economics to be competitive," says Pirates President Mark Sauer. His suggestion: wealthy teams sharing revenues with poorer teams, an idea owners can't agree on after three years of argument.

It's not just the basket cases that are hurting. The Houston Astros gave away tickets at the beginning of the season, and Florida Marlins owner H. Wayne Huizenga was selling \$1 seats in September. The powerhouse Atlanta Braves signed only two new sponsors this year—barely replacing those lost during the strike. The Chicago Cubs, in the playoff hunt through the end of September, will probably lose \$15 million this year, team insiders say. "This season has been a cold shower for players

and owners," says Colorado Rockies owner Jerry McMorris, whose team continued to win in the box scores and on the field.

Now it's looking as though 1994 is not so much a hangover from the strike as a harbinger of what's ahead. Talks have moved nowhere since they resumed in mid-May, and sources on both sides concede that major

agreement isn't likely until next year, when spring training looms. And with the coming breakup of The Baseball Network joint venture among baseball, Capital Cities/ABC Inc., and NBC, the league has to negotiate a new deal even though it can't guarantee a strike-free 1996 season. The trouble with baseball is they can't repair the damage they've done, says Stanford University economist Roger Knoll, who has worked as a consultant to the players' union.

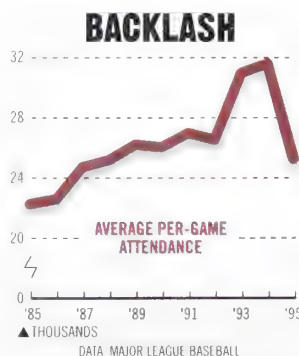
There's little time to waste. If teams start selling 1996 advertising time as soon as 1995's last game is called, the uncertain labor and bleak cast outlook will have an immediate impact. Worse still, some of baseball's core problems—slumber-inducing game length, a nonexistent marketing strategy, listless local sales, and the rich club/poor club chotomy—won't be addressed in

**CLEVELAND NOW PLAYS ONLY TO LOCALS** the league is preoccupied with labor television troubles.

For many fans, the most immediate frustration is the league's decision to broadcast playoffs regionally rather than nationally. Baseball Network officials declared before the playoffs that the network would satisfy fans with frequent score updates and cameos of paced action from games played in the regions. It certainly did not satisfy Cleveland Indians fan David H. Resler, an economist of Nomura Securities International Inc. in New York. The team had gone since 1948 without a playoff win—16,816 games—and Resler couldn't

catch their Oct. 4 victory over Boston. "I saw it through every channel I have," Resler says. "This stinks. It's bad for baseball. It's time when they need something that unites the fans." Not enough. Baseball's growing fan alienation down to fine art.

By David Greisler  
Atlanta, with Steve Baker in Pittsburgh



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EDITED BY THANE PETERSON

## CULLING ORANGE COUNTY CULPRITS?

JUST TWO WEEKS AFTER THE California legislature gave Orange County a reprieve from its budget crisis, the Securities and Exchange Commission began knocking on the door. Sources say that in late September, the regulator sent out notices to people and firms involved in debt issuance in Orange County in the summer of 1994. The sending of the notices indicates that the SEC is in the last stages of deciding if anyone should be charged with fraud. A source confirms that Robert Citron, former county treasurer, has received one. Most of the Wall Street firms that underwrote the issues said to be under scrutiny, in-

cluding Merrill Lynch, CS First Boston, and Rauscher Pierce Refsnes, and the county itself declined to comment. PaineWebber says it has received no notices.

## A BIRD IN THE HAND

TORONTO DEVELOPER PAUL Reichmann always said he would win back the massive Canary Wharf office complex in London. On Oct. 2 he may have achieved his goal when newly formed International Property, with Reichmann as president, agreed to ante up \$1.2 billion to buy the property from the 11 banks that have owned it since the collapse of Reichmann's Olympia & York Developments. Reichmann and his family are buying a 5% stake for \$60 million. Most of the rest of the money is coming from CBS Chairman and Reichmann friend Laurence Tisch, investor Michael Price's fund-management group, and Saudi Prince Alwaleed bin Talal bin Abdulaziz Al Saud.

## GENENTECH'S HANDS ARE CLEAN

BIOTECH PIONEER GENENTECH and distributor Caremark International seem to have put another scandal behind them. On Oct. 3, Vice-President Edmon Jennings and three executives of Caremark were acquitted in a Minneapolis district court related of all charges to alleged Medicare/Medicaid violations. Without waiting to hear defense arguments, the judge ruled that the prosecution failed to prove that the men had played any illegal role in a kickback scheme to promote sales of Genentech's human growth hormone. In July, when Genentech's board ousted CEO Kirk Raab, there was speculation that the case was partly behind the direc-

HEADLINER: JOHN AKERS

## AKERS AND HANSON—TOGETHER AGAIN

Former IBM Chairman John Akers has kept a low profile since being pressured by shareholder activists to step down in 1993. But his latest gig shows a real knack for letting bygones be bygones. In late September, Akers joined the advisory board of Directorship Inc., a Greenwich (Conn.) consulting firm that advises corporate boards on directors' legal responsibilities, pay, and other issues.

Akers goes way back with at least one fellow member of Directorship's board, Dale Hanson. The former CEO of the California Public Employees' Re-

tirement System may have contributed to Akers' ouster: While at CalPERS,

Hanson put pressure on IBM's board to do something about the company's poor performance. "We tried to get as diverse a group of people as we can," says Peter Garrett, publisher of

the consulting firm's newsletter, *Directorship*. What will Akers, who also serves on the boards of PepsiCo Inc. and the New York Times Co., add? "The experience of 35 years in business," Akers says. "I don't have anything else to say."

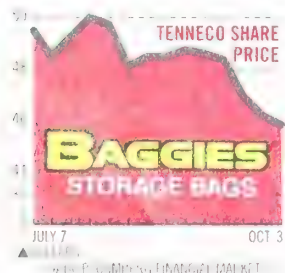
By Elizabeth Les



## CLOSING BELL

### PACKAGING PLAY

Will Tenneco bag higher profits from plastics? On Oct. 2, the Houston company said it would spend \$1.27 billion to add Mobil's Hefty Bags and Baggies products to its packaging division, a business expected to generate 32% of total operating profits of \$1.5 billion this year. The move came on top of asset sales and other restructuring moves. But Tenneco shares are still 9% off their late July trading range of 50. Analysts say investors are concerned about competition faced by Tenneco's natural-gas unit.



tors' move, even though the company itself was not charged.

## ANOTHER ASTROLINK ASPIRANT

LOCKHEED MARTIN JOINED THE race to establish a global satellite system to provide data, voice, and video communication. Astrolink, the \$4 billion project, would put up nine satellites by 2000 to meet the demand for global networking. The company will be competing against Microsoft founder Bill Gates, General Motors' Hughes Electronics unit, and Motorola.

## ONE-STOP SHOPPING ON THE NET

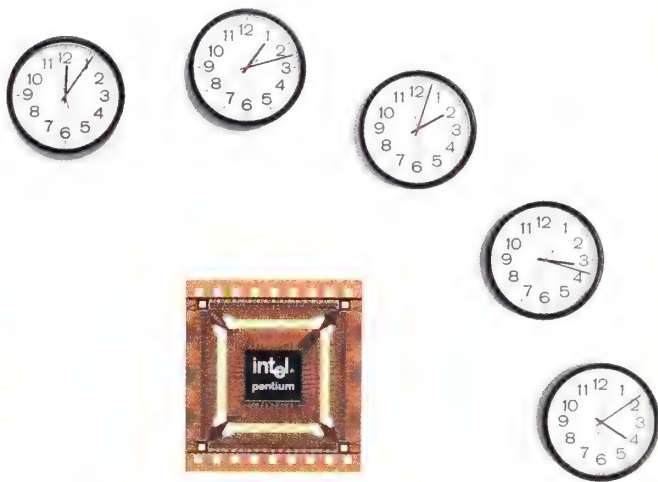
U S WEST PLANS TO ANNOUNCE on Oct. 11 a venture with high-tech all-stars Microsoft, Cisco Systems, Netscape, and Lotus Development to try to

take the lead in market Internet services to clients. The idea: to create a one-stop shop for companies that want to do everything from setting up pages on the World Wide Web to sending sensitive data over the Net to suppliers. "This is a huge new front," says Executive Vice-President Catherine Hapka, who is leading the effort. Some analysts say U S West has done more legwork than AT&T, MCI, and BellSouth, which plan similar services.

## ET CETERA...

- Germany says ex-Barings trader Nick Leeson cannot be extradited to Singapore.
- David Rockefeller is in bidding for landmark Rockefeller Center.
- Is Craig McCaw next? CEO Wayland Hooper abruptly resigned.
- Former Apple exec Jonathan Ive launched a new PC company.

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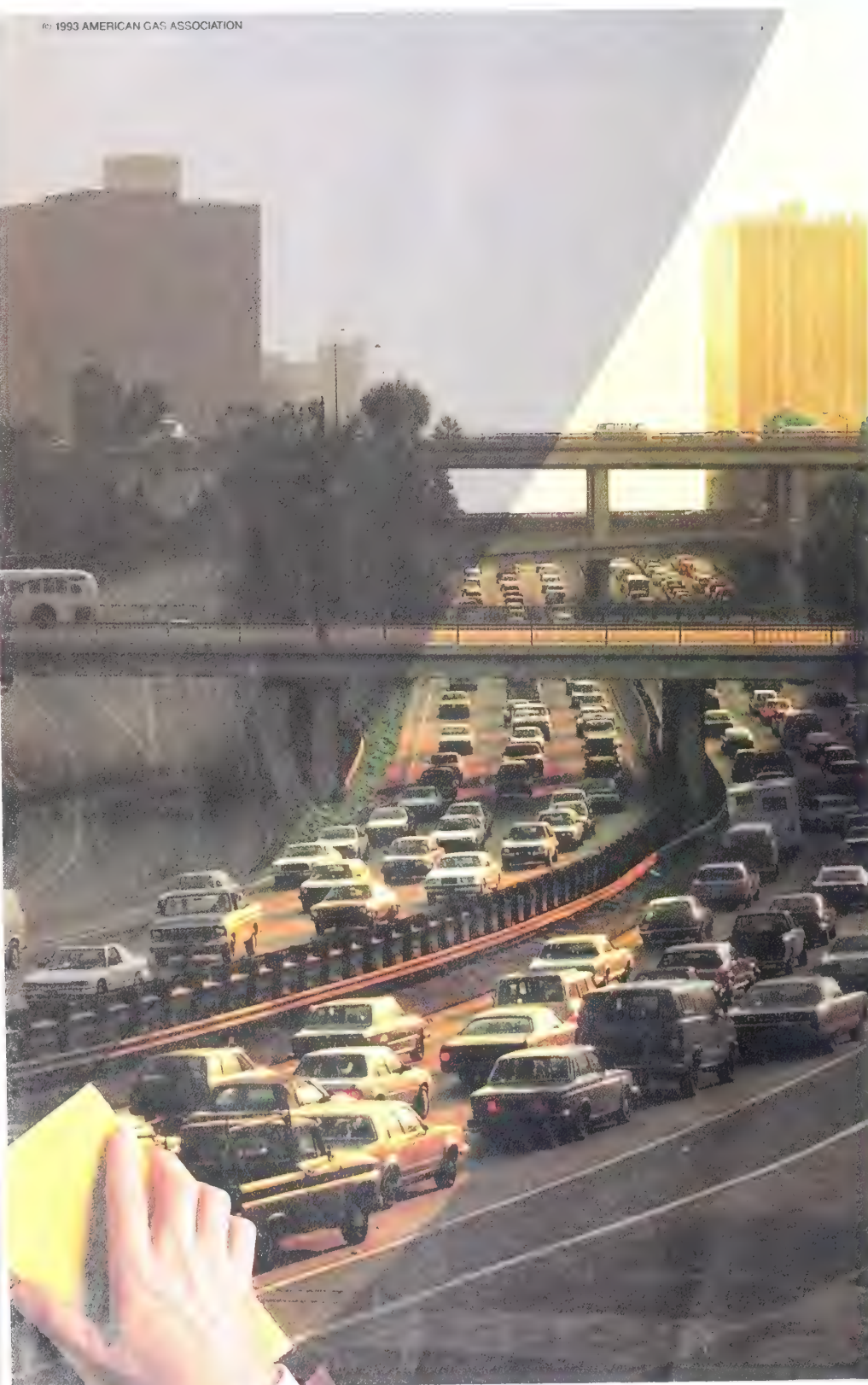
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BY OWEN ULLMANN

## THE WORLD BANK'S LONELY DEFENDER

When it comes to global networking, new World Bank President James D. Wolfensohn is in a class by himself. Good thing, because he'll need every golden connection Rolodex to stave off an assault on the beleaguered international lending agency by Capitol Hill Republicans.

Head of his own Wall Street investment bank until spring, the 61-year-old Australia native rubbed elbows with potentates of commerce and government alike. So he'll be right at home when officials from 178 nations converge on Washington for the World Bank's annual meeting on Oct. 1.

But much of Wolfensohn's schmoozing is aimed at shoring up global support for the International Development Assn., a \$10-billion, interest-free lending program for the world's poorest nations. Why? GOP budget-cutters in Congress are likely to halve the \$1 billion annual U.S. contribution to IDA—something that Wolfensohn warns could throw the whole field of development in turmoil.

**CASUALTIES.** Such warnings matter little to Hill conservatives, who are salivating at the chance to weaken multilateral institutions such as the World Bank. Many Republican lawmakers are neo-isolationists who view the bank as a tool of world-government types. And free-marketters, they also resent multilateral lending. And given the current imperative to rein in spending, foreign aid is a prime candidate for cuts.

But the casualties go beyond IDA. Congress also plans to slash U.S. funding for the African Development Bank and to reduce pledges to a similar Asian fund. "We can't ask people in this country to sacrifice while we're fully funding the needs of Third World countries," says Representative John Dingell (D-Mich.), who chairs the House appropriations committee for foreign operations.

For Wolfensohn, much more is at stake than federal dollars, however. Since the end of World War II, there has been a bi-

partisan consensus in the U.S. to be the lead sponsor of international lending institutions, if for no other reason than to assert American influence around the globe. Now, if the U.S. abandons its commitments, other donor nations will follow suit, Wolfensohn fears. Already, France and Germany are threatening to cut off future IDA funds and form a Eurocentric program—which could cut U.S. suppliers out of procurement contracts. That scenario gives World Bankers the willies. "This could be disastrous," frets Eveline Herfkens, a Dutch member of the bank's executive board. "If the U.S. is not going to foot its share of the bill, it could be impossible to sustain the framework for multilateral lending."

**NEW PET.** Congress' reluctance to cough up aid for IDA also may spell trouble for a new Wolfensohn pet project. He had hoped to use the annual meeting to lobby for a debt-forgiveness fund for the poorest nations, such as those in sub-Saharan Africa. But the new plan is drawing flak from bank and government officials who fear that financing for a new aid project would simply suck funds from existing programs, including IDA.

Democrat Wolfensohn has lined up one powerful ally: Bill Clinton. When Senate GOP leaders asked the Administration how it would allot an uncommitted \$440 million in foreign aid, the President suggested that nearly half go to IDA. Hill staffers see Wolfensohn's velvet touch at work: In August, he threw a bash for Clinton's 49th birthday at his vacation home in Jackson Hole, Wyo. "Now we know the value of hosting a birthday party for the President," muses one House GOP staffer.

But Wolfensohn, an accomplished cellist, will find Hill Republicans much harder to play. Wolfensohn's success at the World Bank depends on his ability to win over critics—who increasingly think the bank is out of tune with the times.

*By Dean Foust*



**WOLFENSOHN:** *Gold Rolodex*

## CAPITAL WRAPUP

### WHAT DO YOU DO?

Everyone knows what Steven Spielberg does—except, apparently, President Clinton's reelection committee. Hollywood mogul is among many well-known Presidential donors whose occupations are missing from a list of 1995 contributors. Federal law requires campaigns to make a "best effort" to describe donors' jobs, but information was excluded for benefactors as Edgar Bronfman, president of Joseph E. Seagram & Sons Inc.; lobbyist Roy M. Neel, Clin-

ton's former deputy chief of staff; and Swanee G. Hunt, ambassador to Austria. After the Federal Election Commission griped, the Clintonites promised to ask donors for more data.

### CEOs LOVE A MAN IN UNIFORM

►Do CEOs want a fellow exec in the Oval Office in '96? Not according to a straw poll at a Sept. 28 BUSINESS WEEK conference in Washington. Only 5 of 90 CEOs named Forbes Inc. chief Steve Forbes as their Presidential pick. The top choice: retired General Colin Powell, with 37 votes. Senate

Majority Leader Bob Dole (R-Kan.) was a distant second, at 17 votes.

### A SHOCK FOR UTILITIES

►The House, concerned that local utilities are gouging the Defense Dept., voted to end electric utility monopolies on Pentagon contracts. Rival energy companies say if they could bid, the Pentagon would shave its \$2 billion annual electricity tab by more than 10%. But contract-holders are fighting the bill in the Senate by warning that lost military business will drive up residential rates.



## CHINA

# THE NEW TRADE SUPERPOWER

China's U.S. surplus is soaring, and its markets are rigged

**O**n the political front, U.S.-China relations seem headed for a thaw after a long, frigid summer. The rapprochement ranges from new U.S. reassurances that it won't upgrade relations with Taiwan to Chinese promises to halt a sale of nuclear equipment to Iran. President Clinton even plans to meet with Chinese President Jiang Zemin in late October in New York.

When it comes to economic issues, however, there's trouble ahead. China's trade surplus with the U.S. is expected to hit a record of \$40 billion this year. And if current trends continue, China will surpass Japan's \$66 billion surplus with the U.S. before the end of the decade.

**DISDAIN?** In fact, U.S. economic policymakers believe that China may have already eclipsed Japan as America's No. 1 trade headache. China's quasi-socialist mega-economy combines a mercantilist industrial policy with disdain for international norms, critics say. "I see a problem of immense proportions," says one senior Clinton Administration official. "[China] is a far more formidable economic concern for us than Japan."

Why are U.S. officials coming to this sudden recognition? One reason is the massive relocation of export industries from Hong Kong, Taiwan, and South Korea onto the mainland. Virtually the entire Hong Kong toy, watch, and garment industries are now in China. Taiwanese producers of Nike and Adidas shoes also have shifted output to China. The latest wave

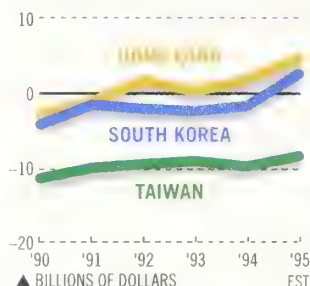
of relocations features compact-disk players, cellular phones, portable stereos, and personal computers. That's partly why U.S. trade imbalances with Asia's Tigers are improving, while the deficit with China is worsening (charts).

It's also increasingly clear that the Chinese intend to use American and European investments to put themselves on the map in such export industries as autos and auto parts, semiconductors, and telecommunications gear. Ford Motor Co. says its new venture with Jiangling Motors Co. will produce minivans, not only for the Chinese market, but also for sale overseas. As Ford and General Motors Corp. compete for a \$2 billion Shanghai family-sedan joint venture, they are both investing in the Chinese parts industry, raising the chance that Chinese vehicles and parts will reach international standards.

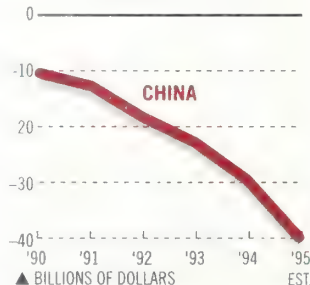
In short, China's export surge is just getting into gear, and already the surpluses with the U.S. have reached painful levels. That's a problem for Clinton, who has made opening markets the centerpiece of his foreign policy. U.S. officials' biggest worry: a vigorous assault next year on China's most-favored-nation trade status by an alliance of China critics and economic nationalists on Capitol Hill. "MFN is going to be in real jeopardy next year if China doesn't open its doors more to U.S. companies," says one political adviser.

The stakes for U.S. business are enormous. China's sheer size makes it impossible for multinationals to ig-

**U.S. TRADE BALANCES SCORE SOME ASIAN GAINS...**



**...BUT THE DEFICIT WITH CHINA IS WORSENING**



DATA: U.S. COMMERCE DEPT., BW ESTIMATES



nore. "Any international company that's not planning to do something in China is probably missing a bet," says J. Patrick O'Rourke, CEO of Varian Associates Inc., a California manufacturer of medical equipment. "It's like the frontier of days past."

But there's a dark side to China, the Wild East. In dealing with problems ranging from opaque licensing requirements to pressure to transfer technology, U.S. executives are discovering that China intends to limit imports while creating new rivals. "The





sponsibilities," says Dana G. Mead, CEO of Tenneco Inc. and chairman of the National Association of Manufacturers.

Conditions for China's entry into the global trade system and other tough issues will come to a head in mid-October when Deputy U.S. Trade Representative Charlene Barshefsky visits Beijing. Barshefsky will turn up the heat on China's leaders to fulfill past pledges to halt counterfeiting of U.S. software, movies, books, and music recordings. She will also press for better access to China's markets for U.S. telecommunications and insurance providers and

countries, all aimed at circumventing U.S. textile quotas. Beijing's crack-down on counterfeiting of U.S. intellectual property has been lackluster, at best.

**ALARM BELLS.** It is the Chinese strategy to enter newer high-end industries, however, that is helping to set off the latest alarm bells in Washington. China used to import up to 10,000 autos a year, placing its orders in high-profile shopping sprees timed for the annual spring debate over MFN. But since the Administration delinked China's trading status from progress on human rights, Chinese officials have virtually choked off auto imports.

Instead, Beijing is pitting Ford, GM, and other big automobile manufacturers against each other in a bidding war designed to transfer technology. "These companies are being pressured to build up their eventual competitors," says Greg Mastel, senior fellow at Wash-

## Beijing is pitting Ford, GM, and other big carmakers against each other in a bidding war designed to transfer technology

ington's Economic Strategy Institute. U.S. trade officials vow to keep the pressure on China to make good on its commitments. Their leverage? Blocking Chinese entry to the WTO until Beijing agrees to play by global rules. Says one top U.S. official: "We cannot allow to happen [with China] what happened with Japan for four decades—sanctuary markets at home and an open U.S. market."

For once, the Administration appears to be speaking with a single voice. At his Sept. 27 meeting with Foreign Minister Qian Qichen, Secretary of State Warren M. Christopher pointedly told his Chinese counterpart that he would have to deal with U.S. Trade Representative Mickey Kantor on trade matters. "It was a way of letting [the Chinese] know there would be no court of appeal" to the usually more sympathetic State Dept., says one U.S. official. Clinton also will have an opportunity to keep trade on the table if he meets Jiang in October. As Washington is starting to recognize, this is one battle that is just beginning.

for elimination of unscientific standards that keep out U.S. wheat and citrus fruit.

Although some U.S. hawks argue that Washington should push much harder, that risks igniting a Chinese backlash. Chinese experts argue the solution is to admit China into the WTO and draw it into a deeper embrace, encouraging it to gradually open protected industries. They warn that any tougher

steps will deepen fears that the U.S. is conspiring to "contain" China. "People are thinking, 'The Americans keep asking for more and more,'" says Hai Wen, deputy director of the China Center for Economic Research at Beijing University. "This is becoming interference in our national independence."

But Beijing also has made a bad situation worse through its own failings. It hasn't been able to effectively police transshipments of textiles. Huge quantities of clothing made in China are relabeled "Made in Hong Kong" or other

are 10 years behind us," says one tech executive, "but if they can us to take on partners and ex-our production, they'll build up the ology and capital eventually to ete with us."

at's why Corporate America is square behind the Administration's ence that China should be allowed in the new World Trade Organiza-WTO) only if it agrees to accepted national commercial rules. "We want them to be at the party ut meeting their real global re-

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But Beijing also has made a bad situation worse through its own failings. It hasn't been able to effectively police transshipments of textiles. Huge quantities of clothing made in China are relabeled "Made in Hong Kong" or other

By Amy Borrus in Washington and Pete Engardio in Hong Kong, with Dexter Roberts in Beijing



## RUSSIA

# THE CONGLOMERATE IS ALIVE AND WELL IN RUSSIA

A strong new industrial-financial combine could give nascent capitalism a big boost

**W**hen defense budgets started shrinking during the late 1980s, managers of Moscow's elite Khrunichev missile factory saw the writing on the wall: diversify or perish. Their first move was to import computers and stereos for resale to goods-starved Russian shoppers. That import business has since evolved into privately owned Microdin, a conglomerate that today controls an impressive 150 companies, including such biggies as jet engine maker Perm Motors and auto and truck producer Zil.

Now, taking another giant step, Microdin will merge next month with a bank-controlled holding company called Interros (table). The combination will create an industrial-financial conglomerate with all the cross-holdings and potential clout of a South Korean *chaebol*. The Yeltsin government has been pushing for just such groups for nearly two years. The idea is that industries with common interests would be linked to banks that could pick up the financing slack from the state.

**A REMAKE.** A behind-the-scenes fight is already brewing over the role of the 23 new financial-industrial groups already formed. The more conservative elements want them to serve as a haven for change-resistant managers left over from the Soviet era. Indeed, critics say the groups that have been formed so far are weak and ineffective, created by Kremlin decree and owning mostly decrepit, nearly bankrupt factories. In contrast, the Interros-Microdin combination could herald a bold new way to marshal Russian capital to remake essential industries. "This looks very good," says Andrei Volgin, head of the Moscow Committee for Shareholders

and usually opposed to such unions. "They combine their financial strength with good industrial assets."

The Microdin merger involves some of the best-known Russian companies and banks. By plowing profits into new businesses instead of parking them in offshore accounts, the former missile men have built up a stable of companies ranging from retail stores and real estate to banks and insurance companies. For its part, Interros is a year-old hold-

making it the third-largest Russian bank; IFC is worth \$1.9 billion. Microdin wedding has even caught the eye of foreign analysts. "Probably two of the three smartest Russian companies are Oneximbank and Microdin," says Charles Ryan, an analyst with Moscow's United Financial Group.

The new holding company will be formed next month. It will be capitalized at \$44 million and initially have assets of about \$450 million. Vladimir Potanin, president of Oneximbank, will serve as chairman, with Microdin President Alexander Efanov as deputy. "These guys really believe in Mother Russia," says one Western analyst in Moscow. "They want to show that they can run companies without foreign help, that they can do it on their own."

Neither man is inclined to sit on assets. Instead, their strategy is to identify potential national champions, snap up shares, pour in money, fire old-time bosses, and stick in modern ones. "The goal of the new holding company," Efanov says, "is to create competitive spur investments, and upgrade management to European standards."

**HARD HIT.** At this, Microdin has already established a track record. In 1993, Microdin and its related companies acquired a 28% interest in Perm Motors, which was also hurt by defense spending cuts and by Soviet-style management. Microdin slashed the workforce from 41,000 to 25,000 and placed in charge one of its own tenants, 32-year-old Mikhail A. Makarov, an aviation engineer. Executives at Pratt & Whitney, the U.S. aircraft engine company, say privately that Microdin pretty much saved their \$125 million joint venture to make commercial

## THE PARTNERS IN A KEY MERGER

*In a \$44 million deal, Microdin, a fast-growing private company, is creating a financial-industrial conglomerate by merging with Interros, a holding company controlled by Oneximbank, the country's third-largest bank with assets of \$3.7 billion*

**INTERROS** Owns stakes in 23 companies in metals, food, chemicals, railroads, and banking.

**MICRODIN** Controls 150 companies in retailing, real estate, banking, construction, jet engines, autos, and trucks.

DATA: BUSINESS WEEK



**CHAIRMAN:** Interros' Potanin



**DEPUTY:** Microdin's Efanov

ing company with stakes in 23 companies, primarily in metals and transportation, including such blue-chip outfits as Norilsk Nickel.

Interros has rich parents. They are Oneximbank and an affiliated unit, Moscow-based International Financial Co. (IFC). Formed by Russian petroleum and metals exporters frustrated by the dearth of trade financing in 1993, Oneximbank has shot to banking stardom. Its assets have ballooned to \$3.7 billion,



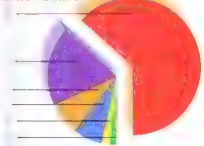
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Director

<sup>1</sup>Jeep is a registered trademark of Chrysler Corporation.

<sup>2</sup>Based on Strategic Vision Inc.'s '95 Vehicle Experience Study of over 31,000 new vehicle buyers during the first 90 days of ownership.

its quality by 26  
over the past three  
measured by reported  
conditions). The  
also won Strategic  
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odge Neon, Plymouth  
Dodge Ram Pickup.\*  
quality will always be  
obsession. It's  
and of commitment  
ains why Chrysler  
on's owner loyalty is  
lay than it has been at  
n its recorded history.  
he financial end,  
s accomplishments  
equally impressive—  
rd operating profits for

1993 and 1994 to the strongest  
balance sheet in its history. This  
financial strength will provide  
for growth at  
home and abroad and see the  
Company through future  
downturns. Chrysler's share-  
holders also are benefiting from  
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Other ventures,  
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tend office con-  
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popular retail  
chain, which  
5 outlets in  
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department  
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paneled Micro-  
let on Berezh-  
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he process, Microdin has estab-  
a distinctive corporate style that  
es youth with brains, energy, and  
alism. The average age of its top  
ship is just 35. Some of them are,  
y, rocket scientists—graduates of  
so prestigious Moscow physics  
athematics institutes who served  
time at the Khrunichev missile  
Efanov is 38 and is trained as a  
ist.

is hunt for acquisitions, the new  
g company will mix Microdin's  
erial skill with Oneximbank's



**SHOPPER'S DREAM:** Microdin's Moscow store features luxury goods and a company-owned bank

deep pockets. Prime targets will be  
companies that have export potential  
and are involved in metals and high-  
tech production. However, they won't  
be looking at oil and gas companies.  
"One reason," says an Oneximbank of-  
ficial "is that the energy field is already  
divided up."

**TAKEOVER BAIT.** Instead, the list in-  
cludes aluminum and steel plants in cen-  
tral Siberia, an aircraft plant in Irkutsk,  
and northern Russia nickel producer  
Norilsk Nickel—one of 29 companies  
whose state-owned shares are slated to  
be auctioned off by yearend. One top  
takeover candidate is Lomo, the former  
Leningrad Optical Factory. Russia's  
largest optical equipment plant, the fac-  
tory churns out everything from medical  
microscopes to night-vision devices for  
the military. An Oneximbank official  
says the new holding company may  
plow in money to modernize the St.

Petersburg plant. Lomo spokesman Vla-  
sic Zalmanov says his company has close  
financial relations with Oneximbank but  
hasn't yet been formally approached for  
takeover.

Given the grand plans, critics worry  
that the new group may not be able to  
manage its disparate units. And share-  
holder activist Volgin says the union  
was spurred in part because Microdin's  
assets were overextended and took a  
beating in Russia's recent bank liquidity  
crisis. Microdin officials deny that.

Whatever the immediate problems,  
the new holding company's example is  
likely to be repeated as Russia's nascent  
securities sector grows more sophisti-  
cated and privatization plows ahead. Se-  
curities analysts in Moscow believe that  
1996 will be a year for mergers and ac-  
quisitions. Look for Potanin and Efanov  
to lead the pack.

*By Peter Galuszka in Moscow*

Microdin has established a distinctive corporate style  
that combines youth with brains, energy, and nationalism



## EUROPE

### GE CAPITAL'S GRAND TOUR OF EUROPE

The company is ravenous for overseas properties

This summer, Gary C. Wendt sacrificed his usual exotic treks to Nepal or up Mt. Kilimanjaro. Instead, the chief executive of GE Capital Services Inc. took a bus trip through Central Europe, visiting Dresden, Krakow, and Warsaw. He also stopped in smaller villages to learn firsthand how life has changed since the fall of communism.

The lessons may come in handy. In the past 10 years, GE Capital has emerged as the most diversified and profitable financial-services company in the U.S. Now, as the company ramps up its expansion overseas, it's redoubling its efforts in continental Europe. This year alone, Wendt's lieutenants have acquired European businesses with combined assets of about \$3 billion (table). They include two German reinsurers, a French consumer-finance company, and a Polish bank. Currently, GE Capital is eyeing Hungary's state-owned Budapest Bank and its \$1.5 billion in assets.

**ECONOMIES OF SCALE.** Europe is fertile ground for GE Capital. With its AAA credit rating, which allows borrowing at favorable rates, and its highly automated operations, which keep down processing costs, GE Capital has a shot at becoming the region's low-cost provider of financial services. Wendt's latest buying binge in Europe is aimed at tying more assets into the network, thus reaping even greater economies of scale. "If they go on this way, they will arise as a very powerful group in Europe," says Gerhard A. Koning, head of corporate finance at Commerzbank in Frankfurt.

Competitors aren't just lying back waiting for the Connecticut bulldozer to run them over. In Britain, for example, Barclays Mercantile Business Finance Ltd., a leader in finance leasing, is cutting costs and improving customer



**WENDT:** The former East bloc is apt to be his next target

service to keep an edge against new rivals. Chairman Tom Clark says that as of now, Germany's Deutsche Bank and France's Société Générale are much bigger worries than GE Capital. But he adds: "Because they're GE, we obviously see them as a threat."

Wendt plans to create a European facsimile of GE Capital's U.S. operations, with 24 different businesses offering everything from car loans to reinsurance. The biggest thrust so far has been in consumer financing, where GE Capital's European profits have risen from nothing in 1992 to an expected \$100 million this year. In auto-fleet management, about a quarter of GE's total of 740,000 vehicles is in Europe. And thanks to the German acquisitions, GE Capital's reinsurance subsidiary, Employers Reinsurance, will soon get half its premium volume from Europe.

Dean Witter Reynolds Inc. and Craig W. Fanning projects that a top of GE Capital's \$315 million earnings increase for 1995, to \$2.4 billion, will come from overseas, principally Europe. That would bring net income in Europe more than \$250 million—a 70% increase over 1994. While he won't confirm numbers, Wendt suggests that may be "conservative." Earnings in Europe have been growing an average 91% a year over the past four years.

GE Capital's recent acquisitions are intended to build on its existing franchises in Europe and expand into areas where the company has yet to make an imprint. These include servicing residential mortgages and bundled services for small to midsize businesses. For example, GE can use its leverage to buy huge discounts on overnight packages, long-distance calling, and office equipment, then resell the service for a profit.

**SAVVY DEALS.** The company got its start in Europe in the early 1990s, when the region was gripped by recession. Under depressed market conditions, GE Capital could gather assets at rock-bottom prices. It picked up the credit-card portfolios of famed British retailer Harrod Ltd., small finance portfolios throughout Scandinavia, and the European commercial-fleet management arm of Avis. One of its savviest deals may have been the 1993 rescue of Irish airplane leasing company GPA Group PLC, which was close to bankruptcy. For just \$1.3 billion, GE Capital bought 45 late-model aircraft and took over management of GPA's fleet. It also snared an option to buy up to 67% of GPA by 1998.

GE's recent interest in Poland and Hungary suggests that the former East bloc is Wendt's next target. With its underdeveloped retail finance services, this market offers even greater opportunities than Europe's maturer countries. GE Capital has made a concerted decision to push into Europe's emerging markets, says Louise Bowler, editor of the trade magazine *Asset Finance & Leasing Digest*. Wendt's expansions to the region have probably just begun.

By Tim Smart  
Stamford, Conn.,  
John Templeman  
Bonn and Peter  
Dwyer in London

#### WHAT GE CAPITAL HAS BOUGHT THIS YEAR

| Total value                                                  |                         |
|--------------------------------------------------------------|-------------------------|
| <b>INSURANCE</b>                                             |                         |
| FRANKONA RE<br>AACHEN RE (GERMANY)                           | \$1 BILLION             |
| <b>CONSUMER CREDIT</b>                                       |                         |
| CREDIT DE L'EST (FRANCE)<br>80% OF SERVICE BANK<br>(GERMANY) |                         |
| SOLIDARNOSC CHASE<br>D.T. BANK (POLAND)                      | \$1.4 BILLION           |
| <b>COMMERCIAL FINANCE</b>                                    |                         |
| PALLAS GROUP<br>(BRITAIN)                                    | MORE THAN \$500 MILLION |

DATA: BUSINESS WEEK



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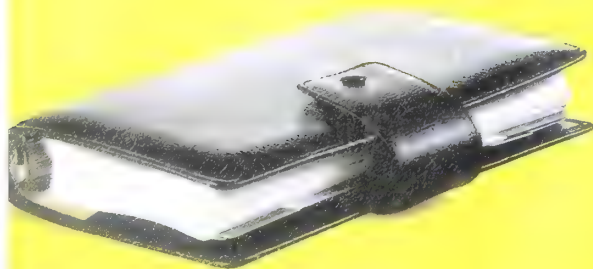


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1992



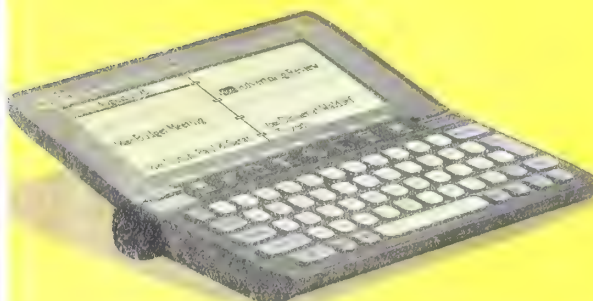
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1994



1995-2049



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EDITED BY WILLIAM J. HOLSTEIN

## WHAT HAS JAPAN AND THE U.S. MAKING NICER? CHINA

The U.S. and Japan pulled out the long knives during their trade dispute over Japan's auto market this summer, at the same time that Washington seemed to be pushing them to painfully high levels. That sense of economic confrontation, greeting the 50th anniversary of World War II's end, appeared to raise the risk of a meltdown of the crucial relationship.

Now, in a change of course, Washington and Tokyo are attempting to achieve a delicate truce. Joint intervention by the Bank of Japan and the U.S. Federal Reserve to rein in hyperinflation has lifted Japan's economic outlook. And even though the June auto pact has been widely attacked as toothless, Washington trade warriors are laying low in deference to President Clinton's summit with Japan's Prime Minister Morihiro Hosokawa beginning Nov. 17 in Tokyo.

Why the new tone? Part of the explanation appears to be the growing concern over China (page 56). Tokyo seems to think that Beijing is starting to show its military heft around in the region. First, Chinese President Jiang Zemin ignored pleas from Murayama toelve a planned nuclear weapons

In retaliation, Japan slashed roughly \$70 million in aid to Beijing this year. It didn't touch the far bigger \$10 billion in development loans China receives.

**FLASH POINTS.** But Beijing then launched tough verbal attacks against Tokyo, a beneficiary of U.S. nuclear protection, dredging up Japan's sordid wartime past. With the hard line coming so soon after Beijing's military exercises off the coast of Taiwan, Tokyo diplomats now openly worry about China's assertiveness. "We have many emotional issues between us," says one senior Foreign Affairs Ministry diplomat. "They could ignite at some point."

The U.S., too, could be attempting to breathe momen-

tum into relations with Japan because of uncertainty over China. With American trade hawks quiet for the moment, the State Dept. and the Pentagon are making a big push to strengthen strategic ties with Japan. They want to use those relations as a building block to draw China into a regional security dialogue.

However, revitalizing U.S.-Japanese relations won't be easy. If Tokyo is counting on security ties to overshadow Japan's \$60 billion-plus trade surplus, it could be in for a let-down. With everything from photographic film to wood imports to semiconductors still on the table, further trade flare-

ups seem inevitable, particularly as the Presidential campaign moves into higher gear. Acting tough with Japan is a political winner at home, and Clinton may be tempted to hit that button.

**DIVISIVE STRATEGY.** There also seems to be a growing inclination to assert self-interest—perhaps even nationalism—in Japan. Even though the Murayama government in late September reaffirmed the effective 70% subsidy Japan pays for keeping 47,000 U.S. troops on Japanese soil, the alleged rape of a 12-year-old girl by three American GIs on Okinawa has raised popu-

list pressures to send at least some of the Americans packing.

Complicating matters is China's keen interest in keeping U.S.-Japanese relations off balance. The reason: That reduces the risk it will face a united diplomatic front in Asia.

In short, the Americans are being drawn into a high-stakes power triangle with Japan and China, reminiscent of President Nixon's use of "the China card" against the Soviet Union. That's why Clinton's meeting with Chinese President Jiang Zemin in New York in late October, followed by his visit in Tokyo, shape up as part of a new great-power game in the world's most economically dynamic region.

*By Brian Bremner in Tokyo*



**IN TOKYO:** *Protesting Chinese nuke tests*

## GLOBAL WRAPUP

### BUSINESS FIGHTS QUEBEC SPLIT

Quebec Premier Jacques Parizeau is at odds with top business leaders as battle heats up over the Oct. 30 referendum on sovereignty. On Oct. 3, Robert Beaudoin, CEO of aerospace conglomerate Bombardier Inc., named hundreds of Montreal executives that a *oui* vote would have "disastrous consequences" for Quebec's economy. Parizeau retorted that Beaudoin and other "apostles of apocryse" are scaring people to maintain

Quebec's "colonial" status. But business is scoring heavily in the debate. Polls show that Quebecers, who in mid-September were evenly split, now oppose sovereignty 55% to 45%.

### ENRON HAS NEW HOPE IN INDIA

► Enron Corp.'s power project, canceled by Maharashtra state in August, may live yet. As many predicted, the state seems set to renegotiate the \$2.8 billion deal. Talks are expected in response to Enron's offer to make changes, including fuel sources

that would lower the electricity tariff.

But the left-wing Rashtriya Swayan Sevak and other political parties are dead set against renegotiating. The RSS has managed to escalate the controversy into a national debate. Politically, though, the state government—a coalition of India's main opposition Bharatiya Janata Party and the regional Shiva Sena Party—may be making an astute move. Says Anand Kumar, a political scientist at Jawaharlal Nehru University: "It says the BJP is strong enough to handle international forces on its own terms."



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## SOFTWARE

# AFTER WIN95, WHAT DO YOU DO FOR AN ENCORE?

For starters, Microsoft is getting around to conquering consumer software

**P**atty Stonesifer has just moved into her digs at "Redmond West," the new campus for Microsoft Corp.'s ballooning consumer group, located a mile and a half from the software giant's headquarters sprawl. The walls are still bare. A clock sits conspicuously on the windowsill—a reminder of her break-neck schedule. Only a vase of long-stemmed red roses hints at another side to Stonesifer's manifestly Type A personality. Or maybe not. The roses bear a recurring message from her husband: "Stop and smell the roses."

Maybe later. Now is the eve of the all-important Christmas selling season, when 60% of consumer software is sold. Stonesifer, senior vice-president of Microsoft's consumer division, is about to unleash the software maker's second big campaign to capture the minds and dollars of home-PC owners. Just as the hubbub over Windows 95 is dying down, Stonesifer's division is preparing nearly 20 new consumer software programs to give PC owners something to play on those Win95 systems—everything from 3D Movie Maker, which lets kids play director, to Microsoft's first shoot-em-up game, *Fury3*. The group also has new hardware, including a big, egg-like trackball for kids, called *EasyBall*, and a precision joystick, *Side Winder*.

**"SO MUCH UPSIDE."** Stonesifer's division is also diving deeper into cyberspace. It just launched *CarSource*, an online buyers' guide, on the Microsoft Network and the Internet, and three of its new software titles will have online links to fetch updates. Says analyst John Gorton of Van Kasper & Co.: "Microsoft is a force to be reckoned with in consumer multimedia."

No argument there. In just three years, the consumer div. has swelled to more than 800 employees and is expected to end the year with revenues of \$800 million, nearly double those of last year. While that's less than 10% of Microsoft's overall business today, the consumer market is a key growth engine. Why? The corporate PC market—Microsoft's



When Stonesifer took over the consumer group two years ago, Microsoft was a distant No. 4 in the market. Now it's closing in on No. 1

PATTY STONESIFER: CAN SHE CLOSE THE CREATIVITY GAP BY CHRISTMAS?



# Sally leased a new car for 24 months.

# Bobby leased from a competitor for 36 months at a lower payment.

# How come Sally actually paid less?

***With a 24-month Red Carpet Lease, Sally avoided the 12 most expensive months.***

Sally did her homework and discovered the low 36-month payment wasn't the end of her financial liability. Down the road she could face additional costs for repairs and maintenance. However, she discovered she could avoid those pitfalls with a 24-month Red Carpet Lease from Ford Credit.

#### **Protection from unexpected costs.**

Sally can drive 15,000 miles a year and enjoy full warranty protection and Emergency Roadside Assistance with a 24-month Red Carpet Lease. If she drove an equal distance with a 36-month lease, her 36,000-mile warranty\* would run out seven months and 6,000 miles before her lease did. One major repair could wipe out what she "saved" with that 36-month lease payment.

#### **No worry about expensive replacements.**

Sally learned that after 30,000 miles of wear and tear she could be spending additional money on the routine replacement of wear items such as brakes and tires. With a 24-month Red Carpet Lease, she would be into a new vehicle by then.

#### **Generous mileage allowance.**

Sally was pleased to see the standard Red Carpet Lease allowed 15,000 miles a year. Not so pleased to discover many competitors' 36-month leases allow only 12,000 miles and charge 15 cents for each extra mile. Sally would have a staggering \$1,350 tab at the end of a 36-month lease just to equal the Red Carpet Lease mileage allowance. The Red Carpet Lease also lets Sally buy more miles up front at only 8 cents a mile and

refunds extra miles over \$1.00 at the end of the lease that she paid for but didn't use.

#### **No return fee.**

Sally was furious to learn that some competitors' leases require a fee of several hundred dollars just to return the vehicle at scheduled lease end. A Red Carpet Lease has no such fees.

#### **Three pleasant choices at lease end.**

One feature that Sally really liked was that at the conclusion of her Red Carpet Lease, after fulfilling her lease obligation, she still had financial flexibility. She could (1) return the vehicle and lease a new one,\*\* (2) purchase the vehicle at a predetermined price and keep it or (3) return the vehicle and walk away.

#### **A 24-month Red Carpet Lease has clear advantages.**

In the final analysis, Sally discovered it simply costs more to drive for 36 months than it does for 24 months. So, do your homework as Sally did, and you'll see that a 24-month Red Carpet Lease from Ford Credit is a genuine value.

#### **Ford Credit Red Carpet Leases rank first in customer satisfaction two years running.**

In '94 and '95, CNW Marketing/Research found that people with 24-month Ford Credit Red Carpet Leases have the highest level of satisfaction. That could explain why Ford Motor Company leases more vehicles than any other manufacturer.\*\*\*



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# Information Processing

traditional stronghold—is slowing to 10% annual growth, while the home market is surging by 30% a year. Says Chairman William H. Gates III: “The consumer business just has so much upside.”

Until Gates tapped Stonesifer to exploit that opportunity, Microsoft was a success, albeit a minor one, in consumer software without really trying. Microsoft Works and Publisher sold well to the home-office crowd, and Flight Simulator, introduced in 1982, has been a perennial favorite—now owned by 2 million cyber-aces. But in 1993, a year after the consumer div. was formed, sales of home software and games amounted to only \$251 million a year, says market researcher Dataquest Inc. In 1995, it predicts the consumer div. will be the largest multimedia software outfit in the U.S., leapfrogging Acclaim Entertainment Inc. and Electronic Arts Inc. (table). With its hardware sales thrown in—revenue from keyboards, mice, and joysticks are expected to hit nearly \$250 million—the division is on its way

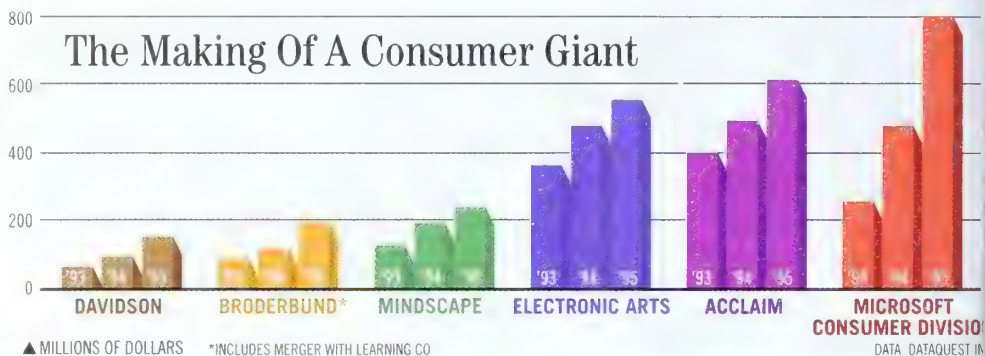
to becoming a billion-dollar baby.

Stonesifer, 39, is not your typical Microsoftie, and that may have a lot to do with the division's success. A former editor-in-chief of Que, a computer book publisher, she spent most of her career in publishing until joining Microsoft in 1988 as senior manager of Microsoft Press. In 1990, she impressed Gates at a management meeting and her big break came. Within three weeks she was the head of Microsoft Canada.

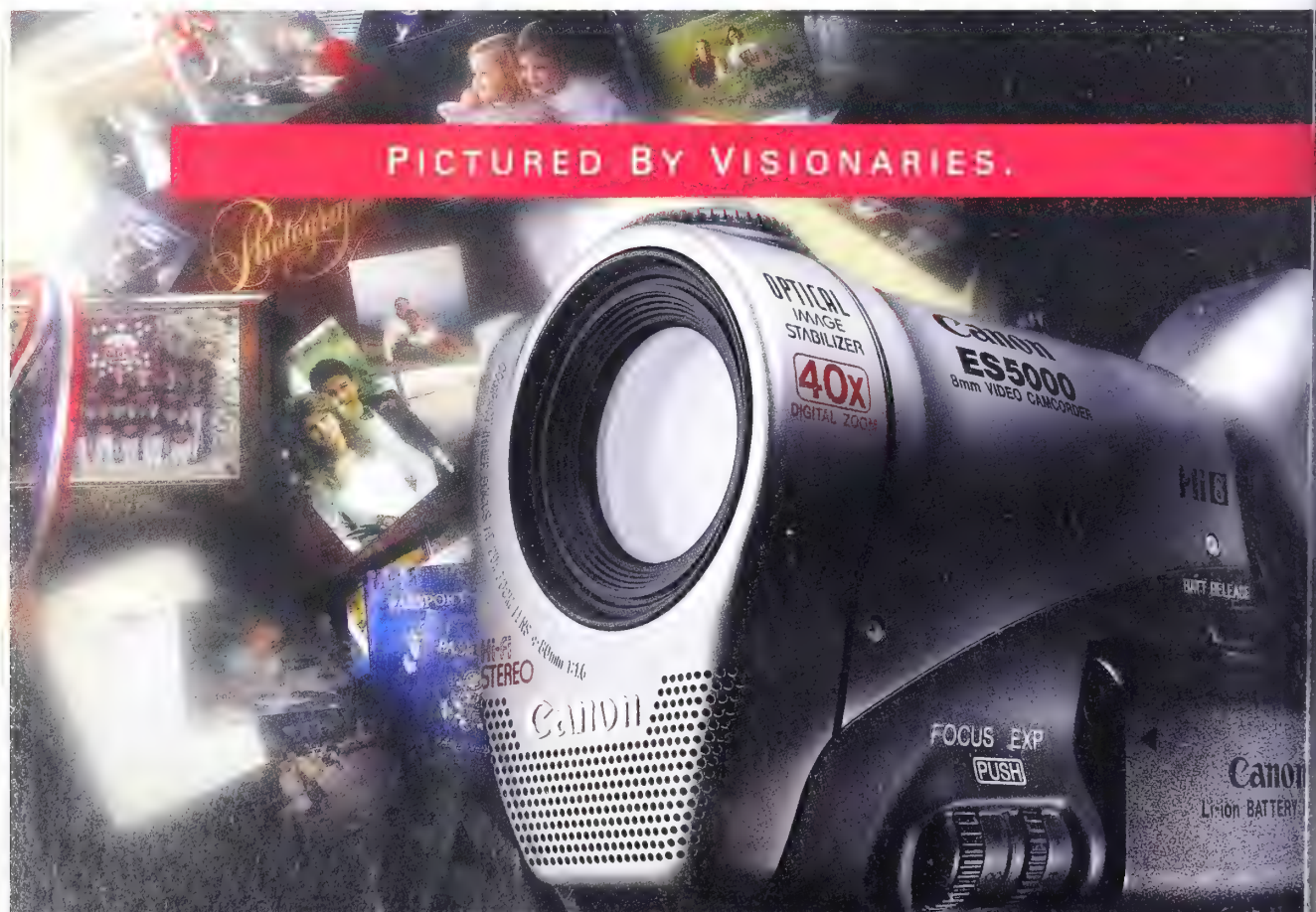
In 1991, Gates summoned her again—this time to fix Microsoft's support center, where customers were waiting on help lines for up to 20 minutes. Two

years later, under Stonesifer's watchful eye, the wait was under 60 seconds—at least, until Windows 95 arrived in August and blew the averages. “Patty is a strong leader,” says Gates. “She's very crisp in how she figures things out.”

Take the consumer div. She took over the unit in the summer of 1993 when it had but 25 products and was a distant No. 4 in consumer software. Today, there are nearly three times that many products and she is closing in on No. 1. Stonesifer quickly realized she would have to do things differently. “Bill really encouraged me to make sure we didn't just replicate Microsoft,” she says.



PICTURED BY VISIONARIES.





helped shape her conception of the new Redmond West facility, where there's lots of shared space and more free-form atmosphere. Without opportunities for casual collaboration, says Stonesifer, "It's always easy to find that great idea." Stonesifer established a unique blend—Microsoft Home—restructured around products (Kids, Productivity, Entertainment, and Information), replacing units oriented around technologies such as multimedia.

Top objective was to move beyond traditional Microsoft mindset so they could match other software companies—particularly makers of computer games—in creativity and entertainment value. To this day, the division's sellers remain productivity programs such as Works and reference titles such as Encarta, a high-end electronic encyclopedia.

That's why rivals aren't too worried. Virtue of its size, Microsoft is a major competitor, says Kenneth F. Gold-

publisher of education and entertainment products for Broderbund Software Inc., which publishes hits such as *Where in the World Is Carmen Sandiego?* and *Myst*. But when it comes to creativity, he says, "Our titles are better, more inspiring, fresher."

**MISFIRES.** Rivals are also happy to note Microsoft's consumer software setbacks. Bob, a heavily promoted whimsical interface to help newbies navigate their PCs, has not been a hot seller. Likewise, Microsoft Money was such a poor seller that Gates attempted to buy Intuit Inc., which produces the leading personal-finance package, Quicken. Gates dropped the bid rather than wait out an

antitrust investigation. The Money team went back to work, and today an improved version of the program is getting raves.

Another dud: Microsoft Baseball, which had the misfortune to be born during the 1994 season, just when the baseball players' strike was alienating ball fans. In games—the hardcore heart of multimedia—Microsoft remained a lowly No. 7 in the first half of the year, according to PC Data.

Microsoft, never a slouch at marketing, has one quick fix: a giant pre-holiday price cut. As of Oct. 1, Microsoft's 50-odd consumer titles, which had been priced at a premium, have been scaled back to match or, in some cases, undercut the market. Now, more than 30 Microsoft programs cost less than \$50; some are selling for \$30.

Stonesifer is working hard to give her division the needed creative talent. She has hired from places such as Disney, Paramount, Lucas, Sony Films, Sega, and Blockbuster Entertainment, and the preliminary results will be visible this Christmas. *Fury3*, a space-age action program, makes you the pilot—



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**MOTOROLA**



# Information Processing

dipping, spinning, and battling enemies to save planets from destruction. Microsoft is counting on *Fury3* to establish its credentials with serious gamers, and early reviews give it a thumbs-up.

On the kids side, there are two promising new titles. One is an addition to the popular Scholastic's Magic School Bus series: *Explores the Ocean*. Wacky science teacher Ms. Frizzle again takes kids on an educational romp, this time through a 3-D sea of giant kelp. And then there is the real grabber: *3D Movie Maker*. Kids can compose animated stories by selecting from a cast of 40 actors that can be seen from 30 dif-

ferent camera angles. It has Gates jazzed: "Of all Microsoft's products I've seen in the last year, whoooa!"

Today there are 75 people in the consumer div. working on at least 10 games, everything from action adventures to espionage thrillers. To increase the odds of creating the next big hit, Microsoft is operating like a Hollywood studio: financing, producing, and marketing titles that are cooked up by independents. Some 90% of Microsoft's games are in the hands of outside developers, such as Larry Holland, who designed the hit *Tie Fighter* game for LucasArts. Magic School Bus programs

have been developed by New York-based software maker Music Pen Inc. in conjunction with Scholastic Inc., publisher of the book series.

Of course Microsoft still counts heavily on technology to make all this creativity come to life. It is spending an estimated \$10 million to build a 20,000-square-foot production facility that George Lucas would admire. This "catal backlot" will have suites for syncing sound, a recording studio, video editing suites, and a digital imaging lab. "I heard before I came here it was a stodgy place," says Larry Frame, a re-

## Coming to a Christmas stocking near you

*To boost its chances of having a holiday hit, Microsoft is using both outside and in-house developers*

▼ A NEW MAGIC SCHOOLBUS TITLE WILL FEATURE 3-D VIDEO

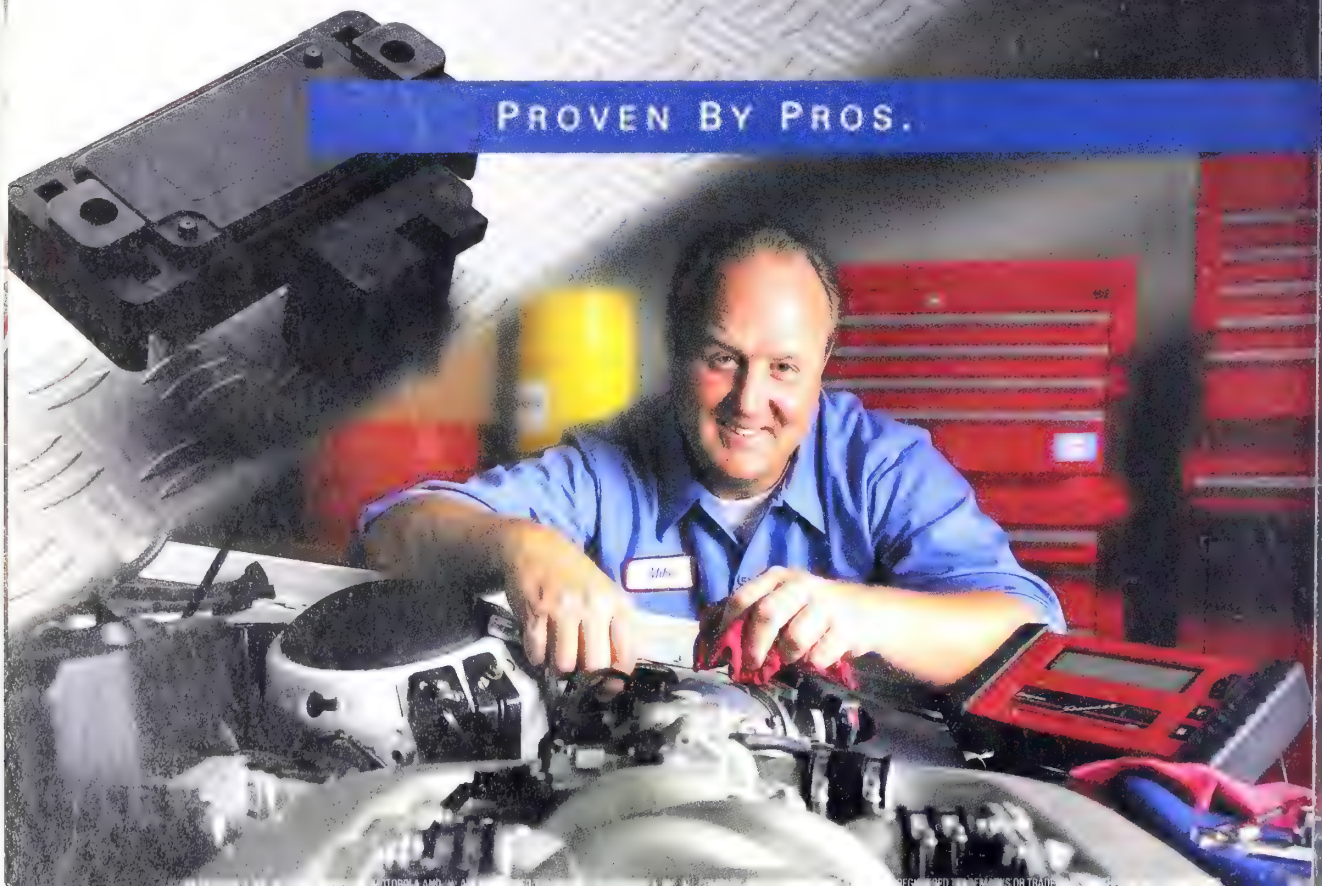


▲ OCEANS TAKES KIDS ON AN INTERACTIVE TOUR

▼ GOLF GOT A FACELIFT FOR WINDOWS 95



PROVEN BY PROS.





Paramount executive who joined Microsoft eight months ago as manager of the digital backlot. "But Microsoft's commitment to creativity, and this is proof of it."

The company is eyeing a 50,000-sq-ft facility in Redmond for a sound stage. And then there's "Blender," set up earlier this year. It's a blend of artistic and technical talent—industrial designers, an illustration director, photographer, and user-interface expert—dream up ideas for interactive TV. They also test multimediated programming on different types of hardware. Says Charlotte Guyman, general manager of the Kids & Games business unit (dubbed KGB): "This is so smart across media: CD-ROM,

online, and NBT—the Next Big Thing."

The Next Big Thing could be putting more consumer programs in cyberspace. CarSource is just the beginning. Nearly every group in the consumer div. is looking into how their titles would play on Microsoft Network or the Internet. Reference works with oodles of information—Encarta Encyclopedia 96, Cinemania 96, and Music Central 96—will tap into the Internet and MSN this Christmas, letting Cinemania owners get fresh movie reviews, for example.

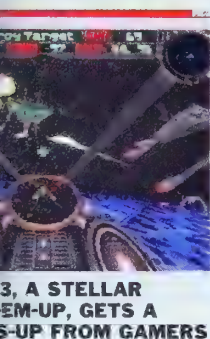
**HOLLYWOOD BOUND.** Next year, Microsoft plans to launch half a dozen online-only products. In two or three years, the company expects only 70% to 80% of its consumer programs will be on CD-ROM. Says Melinda French, general manager of the information business unit and Gates' wife of nearly two years: "Everyone in my group knows the future is online."

Another potential big deal: DreamWorks Interactive, the joint venture between Microsoft and DreamWorks SKG, the startup run by Steven Spielberg, Jeffrey Katzenberg, and

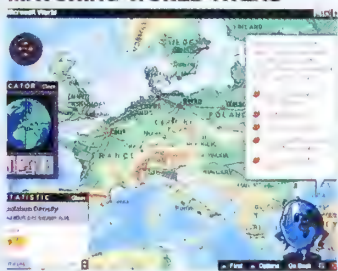
David Geffen. The joint venture has 33 employees working on a dozen games and kids' titles. Executives will only say that they are emphasizing storytelling and will probably use characters from DreamWorks movies. Stonesifer negotiated Microsoft's deal with DreamWorks and is now acting CEO of DreamWorks Interactive. "Patty is that rare breed of executive that can be incredibly focused, decisive, commanding, and compelling—and genuinely have a good laugh along the way," says Katzenberg.

For every story of Stonesifer's relentless drive—she works 12-hour days and answers e-mail on weekends—there's another about her humor and her self-effacing style. Subordinates tell about a tense meeting when she and Gates announced that, because of the Intuit bid, the Money program would be given to rival Novell Inc. After delivering a rousing speech to employees, Stonesifer and one of her executives charged out the door—the door to a closet. Stonesifer laughed so hard she cried as she backed out. Today, she tells that story in management meetings to teach "survival skills." Says Stonesifer dryly: "Nobody's leadership is perfect at any given moment." Perfect or not, this is her moment.

*By Kathy Rebello in Redmond, Wash.*



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## ONLINE SERVICES

### IS DELPHI FINALLY OUT OF THE STARTING GATE?

The Murdoch online service has a new look and new content

**T**here's a dark-horse challenger in the world of online services that could come from behind. With an array of killer "content," huge marketing clout, and vast sums of money at its disposal, Delphi could pull folks into cyberspace by the megadrones—perhaps grabbing large chunks of the market from America Online, CompuServe, and Prodigy.

Delphi? You mean that stodgy, low-tech service that has been around since 1981 and hardly anybody uses? Well, not exactly. This is an all-new Delphi that has been redesigned from the inside out. Two years ago the service, based in Cambridge, Mass., drew lots of attention by becoming the first consumer service to offer complete access to

the Internet, just as the feeding frenzy over that worldwide public network began. The company even changed its name to Delphi Internet Services. But Delphi's screens were text-only—even when perusing the hot, multimedia World Wide Web. As a result, the company lost its Internet lead and is stuck with only 110,000 subscribers—trivial next to the Big Three's millions (table).

Delphi's early move into the Internet, however, did have one major consequence: It caught the eye of media mogul Rupert Murdoch and his vast News Corp. For an estimated \$12 million, Murdoch picked up the lagging service two years ago with hopes of putting News Corp. material—stories from its tabloid newspapers, snippets from

*Mighty Morphin Power Rangers* and other Fox TV shows, photos from *TV Guide* and other magazines—onto the Information Superhighway. News Corp.'s purchase of Delphi excited, though disappointed analysts, who saw few outward signs of progress.

That began to change last summer. In June, News Corp. announced a \$2-billion joint venture with telecom giant MCI Communications Corp., allowing Delphi to merge with MCI's own emerging Internet unit. More important, the combined unit was placed in the hands of Scott Kurnit, formerly No. 2 at Prodigy and one of the executives who had pushed for big changes at that troubled Sears-IBM service.

**ACHIEVING ONENESS.** So far, Kurnit has moved aggressively on Delphi's all-encompassing revamp. The service has moved its headquarters to New York City's trendy Flatiron district, where dozens of multimedia companies have out their shingles. Anthea Disney, the high-profile former editor-in-chief of Murdoch's *TV Guide*, was brought in to head up editorial operations.

The strategy? The new Delphi is seeking to become "one with the Internet." In fact, says Kurnit, the Delphi



REDEFINED BY INNOVATION.

"The sound that issues from this little stereo'radio is startling." Popular Science

## ONLINE RIVALRY

SUBSCRIBERS TO ONLINE SERVICES  
OF JUNE 30, 1995

COMPUSERVE  
3.2 Million

AMERICA ONLINE  
3.0 Million

DATA: SIMBA INFORMATION INC.

ity will eventually fade, to be replaced by a News Corp.-owned Internet service. The reported service is still being tested, but it will likely lure subscribers with low-cost access to the Internet and Web. Kurnit and News Corp. officials won't comment on pricing yet, but Mark Mooradian, an analyst with New York-based Market Communications Inc., speculates that to grab market share the company will charge as little as \$10 per month for unlimited connect time. "Delphi all day has offered unlimited access for as long as it can," he says. "What if they cut out all the Internet access pro-



**LIVE FROM SILICON ALLEY:** Kurnit and Disney

viders and use the MCI marketing muscle to do it?"

However, for all the resources that MCI and News Corp. are pumping into Delphi, analysts are not sure the public will bite. Says Lorraine Sileo, an analyst with market researcher Simba Information Inc., based in Wilton, Conn.: "You can't just throw money at the thing and expect it to work." Like oth-

PRODIGY  
1.35 Million

GENIE  
130,000

DELPHI  
110,000

er Internet access providers, Delphi still needs to figure out how to generate revenue on the "free" Internet. Kurnit is keeping his answer close to his vest. One way would be by linking Delphi Net surfers to Market-placeMCI, an online mall where, using Netscape Communications Corp.'s so-called secure Web-browsing software, shoppers can buy flowers or CDs with a credit card.

Another way to bring in revenue is by selling advertising space on Delphi's home page. If the MCI-News Corp. venture can guarantee a certain "readership," then it can lease out spots that

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would draw surfers to an advertiser's own home page. Delphi had one limited trial of advertising with *Strange Days*, a Fox movie now making its way into theaters. Delphi officials are mum about the test results, however. "We're clearly in the development phase," says Kur-nit. "It's still unclear what percentage of revenues will come from ads and what will come from subscriptions."

The surest way to lure consumers to your corner of cyberspace is the same way you use to get them to read your magazines or tune in to your TV station: by offering lots of attention-getting content. That's where Disney comes in. In addition to putting up links into the various News Corp. media units, such as Harper Collins, Disney is ginning up new online content. She has hired a staff of 20 writers and editors who report and write stories and create features from the Flatiron headquarters—or wherever the news may occur.

**"MASS-ME."** During the recent United Nations' Fourth World Conference on Women, held in China, for instance, Delphi offered commentaries on the conference topic, "Action for Equality, Development and Peace." Such luminaries as Patricia Ireland, president of the National Organization for Women, and Camille Paglia, author of *Sexual Personae* and other works, weighed in. There were also daily first-hand reports, filed by a staff reporter attending the conference in Beijing.

"One of the things that we're trying to do is to make [the service] intimate for consumers," says Disney. The online *TV Guide*, for example, invites Web surfers to submit their own reviews of television programs. And just in time for the fall football season (viewable on the Fox network), the Delphi home page is hosting football trivia contests for Web surfers. And by creating conversational forums and areas geared toward niche interests—ones people are passionate about—Disney thinks that it could generate a massive group of loyal subscribers who will log on to Delphi just to get at the stories they want. "'Me-news' is better than 'mass-news,'" says Disney. "What we want is 'mass-me.'"

While leaping from 110,000 into the multimillions of customers may seem a stretch, analysts say the parent companies' marketing muscle could make it happen. With the millions MCI reaches through its Friends & Family calling program and the pull News Corp. has with its publications and Fox TV, the new Delphi could promote itself all over the place. Which means your next calling circle could include your PC.

By Paul M. Eng in New York

## Science & Technology

### MEDICINE

# NO MORE SNEEZING, ITCHING, COUGHING?

Science is working to prevent allergic reactions

**A** purring cat curled up on an old sofa might seem bucolic, but for many allergy sufferers the scene signals misery: itchy eyes or nose, an uncontrollable urge to sneeze, a tightening throat. Before long, invisible assailants—cat dander and dust mites—send their sniffing victims racing for tissues and antihistamines.

Within a decade, however, the hankies might be gone for good. At laboratories in drug companies such as Genentech Inc. and Ciba-Geigy Corp., as well as in universities, scientists are scrambling to decipher the complicated pathway that leads to an allergy attack. The researchers' discoveries have helped them identify a handful of new approaches to drugs that may halt allergic reactions before the first sneeze. "Where the action is in allergy drugs is not in symptomatic relief but in stopping the allergic process altogether," says Dr. Francis Cuss, vice-president for discovery research at Schering-Plough in Kenilworth, N.J.

Allergies affect nearly 20% of the U.S. population. Some 24 million people suffer from the sneezing and runny-nose variety known as allergic rhinitis. Asthma—which is most often caused by allergies—affects an additional 10 million Americans. Food, insect venom, and chemical allergies plague still others.

**LAND MINE.** There seems to be more of the misery around than ever, too. Sales of prescription and over-the-counter remedies in the U.S. could rise 8% next year, reaching \$4.5 billion, estimates POV Inc., a health-care publishing company in Montclair, N.J. The bulk of those sales

are antihistamines and steroids, which although effective in many cases, are usually taken after symptoms have already begun. Their side effects range from sleepiness to more serious metabolic problems associated with long-term steroid use.

Companies are aiming to capture the huge market with new preventive drugs that could be taken safely for years.

**Drugmakers are trying to attack the underlying cause of the misery: Immune systems that are overly sensitive to allergens**

do that, they are attacking the underlying cause of allergies, which is that the immune systems of allergic people treat such noxious substances as cat dander or mold with a vengeance or usually reserved for viruses or other dangerous invaders. It's still not clear why their bodies are so vigilant, but doctors have identified one main culprit. It turns out that allergic people churn out a lot of an antibody called immunoglobulin E, or IgE, when exposed to allergens. The IgE—which is produced only in minute amounts by people without allergies—attaches to a docking site, or receptor, on so-called mast cells that line the surface of the lung, nose, and other areas.

Once in place, the IgE acts like the trigger on a land mine. When cat dander or another allergen hooks onto the free end of IgE, it causes the mast cell to explode, spewing a potent cocktail of histamines and other substances that lead to the stuffy nose, itchy eyes, and other symptoms of allergies.

One approach then, is to disarm the trigger, IgE. Two companies, Tanox E-systems Inc. in Houston (in a partnership with Ciba-Geigy) and Genentech in South San Francisco, are conducting clinical tests of drugs that do just this. Their approaches are similar and



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## Chapter Three



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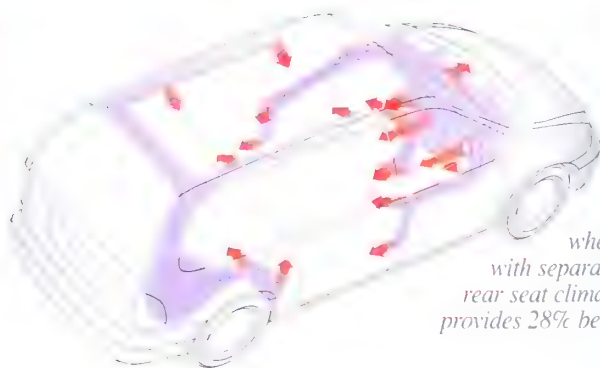


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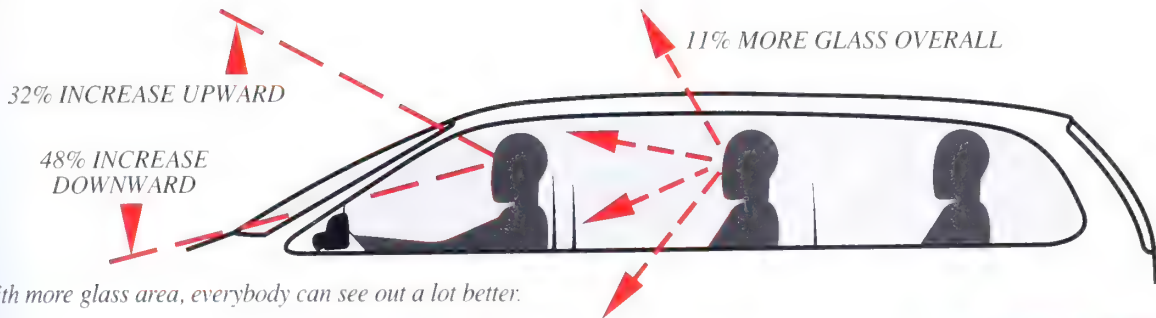


63"

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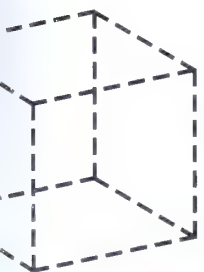


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volve using a so-called monoclonal antibody that specifically grabs onto IgE and prevents it from attaching to mast cells. Tanox' drug not only stops IgE short of its goal, it seems to stop production of fresh IgE. "With our antibody, the IgE in the blood disappears almost immediately," says Tse Wen Chang, Tanox' vice-president for research and development.

Monoclonal antibodies do have limitations. For one, they must be injected—in this case, says Chang, weekly, and possibly for life. Also, because the antibodies are originally derived from mice, there is the possibility that the human immune system could see them as foreign and mount an attack against them.

Still, both Genentech and Tanox estimate that their antibodies

the immune system is still quite new, but Schering's Cuss says that scientists at his company and its affiliate, DNAX Research Institute of Molecular & Cellular Biology Inc., are already working on developing drugs that would target the substance. They would either keep IL-4 from being produced, soak it up once it's been released, or prevent it from attaching to B-cells.

There's some concern, though, that interfering with IL-4 might hurt the immune system's ability to fight disease. "IL-4 is not a mistake of nature," says Dr. Donata Vercelli, a chief scientist at San Raffaele Scientific Institute in Milan and

**DRUGS** that block other immune cells, called B-cells, from getting IL-4's message to produce IgE antibodies.

*Companies: Schering-Plough with DNAX.*

## New Angles Against Allergies

*Most allergy drugs work by mopping up histamines. But several companies are working on drugs that would stop the allergic "cascade" before histamines are produced*



could be available in three years. That is, unless legal wrangling slows the process down. The companies are battling in court over who owns the anti-IgE technology.

**FRANTIC MESSAGE.** Meanwhile, researchers at other labs envision tackling allergies even before IgE is produced. The process starts, they discovered, with the sentinels of the immune system—the so-called T-cells. People who are allergic have a high proportion of particularly alarmist T-cells, says Dr. Marshall Plaut, chief of the allergic mechanisms section at the National Institute of Allergy & Infectious Diseases. When they detect an allergen in the bloodstream, these sentinels send out a chemical message urging B-cells to make IgE. This chemical message is a substance called interleukin-4, or IL-4.

Research into IL-4 and its effect on

**VACCINES** that stop immune cells called T-cells from producing a chemical alarm called IL-4.

*Companies: ImmuLogic with Hoechst Marion Rousel.*

Another approach that targets IL-4 is a vaccine that takes its cue from weekly allergy shots. With allergy shots, people are given very small doses of dander, ragweed, or whatever makes them allergic. The idea is that over time, the person will be desensitized. Recently, researchers discovered that rather than inciting the T-cells to produce IL-4, the constant low doses of allergen actually inhibit its production. Instead, the T-cells make another substance, IgG, that halts the allergic process.

The problem with allergy shots, says Plaut, is that it can take years to get the proper result. That's because there

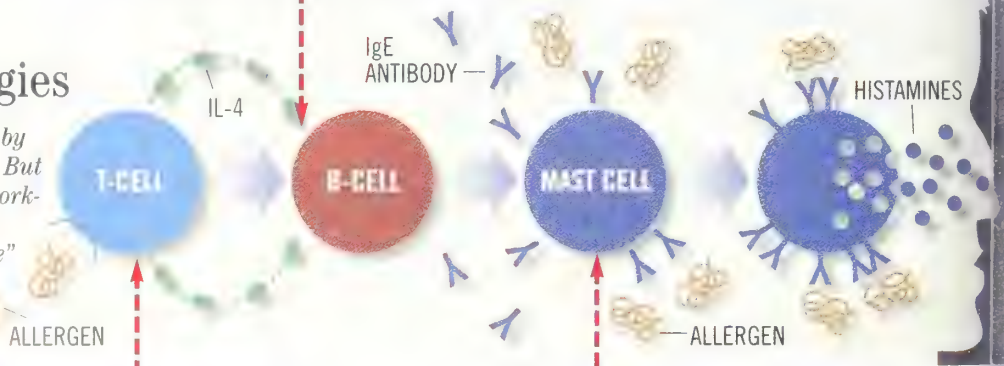
an expert on IL-4. Cuss says the promise of Schering's speculative work outweighs the risk of failure. "If we are right, it is going to be very useful to humans with allergies and asthma, and it will make us a lot of money, too."

**DRUGS** that stop IgE antibodies from attaching to mast cells that line the nose and throat, preventing them from spewing histamine and other chemicals.

*Companies: Genentech, Tanox.*

is a delicate balance between giving a person enough allergen to shut off the immune system and giving so much that it sets off an allergic reaction. To be safe, doctors usually only inject very small doses of the offensive substance into a patient—too small to have a timely effect.

**GENETIC TRAIL.** But scientists at ImmuLogic Pharmaceutical Corp. in Waltham, Mass., have a way around that problem. Instead of injecting the whole allergen, says Dr. Robert J. Gerety, president and CEO of ImmuLogic, "we identified the pieces that can turn on the immune system." These pieces—the allergens—called epitopes—are injected over the course of several weeks, not years. Gerety says clinical trials of the vaccines for cat dander and ragweed are in phase III, or late-stage trials. In earlier tests on the cat vaccine,



some 86% of people who received four weekly injections saw their symptoms abate for several months, says Gerety.

ImmuLogic hopes to begin marketing its first two vaccines—Allervax for cat dander and Ragweed—by early 1998. The company is teamed with Hoechst Marion Rousel to develop the next two vaccines—for house dust mites, Japanese cedar pollen, and grass. So far, Hoechst has contributed some \$40 million to ImmuLogic, says Gerety.

For the time being, the assault on allergies is continuing on two parallel fronts. As companies race to develop the next billion-dollar remedy, academic researchers are identifying the genes that make people asthmatic or allergic in the first place. If they succeed, scientists will be able to intervene even earlier in the allergic process. For allergy sufferers, that's nothing to sneeze at.

*By Naomi Freundlich in New York*

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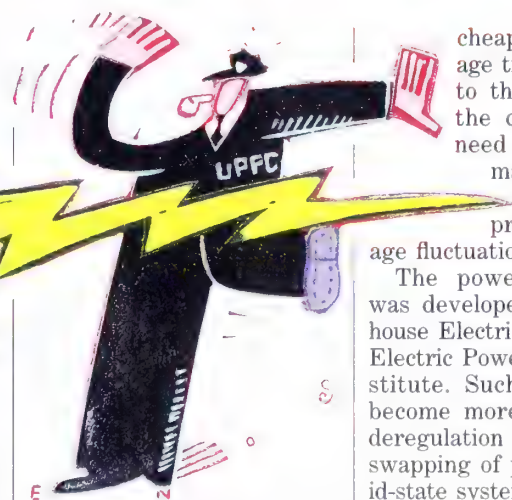
# Developments to Watch

BY PETER COY

## ING CTRICITY TURN A DIME

AMERICAN ELECTRIC POWER needs more juice in northern Kentucky to meet the needs of the state and coal. To supply electricity at the least cost and with least disruption to power transmission in surrounding areas, the utility is contracting a state-of-the-art computer-control system called Unified Power Flow Controller.

The UPFC is the first system capable of simultaneously controlling all the major characteristics that determine power flow over trans-



mission lines. That enables the utility to control power flows instantaneously and precisely. One big advantage is that American Electric Power will be able to build a

cheaper, lower-voltage transmission line to the region, since the company won't need a huge safety margin to guard against unpredictable voltage fluctuations.

The power-flow system was developed by Westinghouse Electric Corp. and the Electric Power Research Institute. Such systems will become more important as deregulation results in more swapping of power. The solid-state systems also take up less room than their mechanical predecessors, which can be as big as football fields. AEP's facility is 100 feet by 150 feet—including a spectator's gallery.

## , CHIPS THAT AN UP THE TIMEDIA MESS

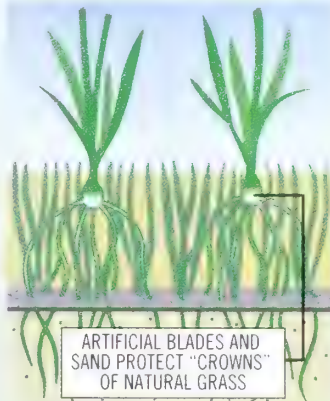
PERSONAL computers are a pain in the neck. You spend hundreds of dollars on add-in cards, and you almost need an engineering degree to install them. Startup Chromatic Research Inc. in Mountain View, Calif., hopes to change that. On Oct. 9, it was to introduce a single chip that does out all major multimedia functions—such as video acceleration, video playback, audio playback, and modem.

The Mpack chip runs with the help of software modules, which can be reprogrammed. Indeed, since Toshiba and South Korea's LG Electronics Co. will manufacture the chip, Chromatic expects to make money mainly from software. Running multimedia on software instead of hardware means the 1.5-megabyte transistor chip can be smaller and cheaper. Chromatic estimates the chip, which requires no additional memory chips, will add about \$150 to the cost of a PC.

## AN ARTIFICIAL ANCHOR FOR REAL GRASS

ROSS C. LITTLE HAS TAKEN AN INTENSE INTEREST IN THE University of Utah's Running Utes football team this fall. Not in whether they win or lose, but in how the grass beneath their feet holds up. Utah's Rice Stadium is the most challenging and conspicuous venue yet for a new kind of turf made by Little's company, SportGrass Inc. of McLean, Va. SportGrass is real grass planted on a synthetic base. The base is a woven fabric with polypropylene blades sticking up, as in a sparse shag carpet. Sand is poured over this to the tops of the blades, and then natural grass is planted on top. The base protects and anchors the vulnerable "crowns" of the grass, where the blades meet the roots. The aim is to lessen the wear on natural grass, which players say produces fewer injuries than artificial turf.

The result? "So far, so good," Utah grounds department supervisor Susan Pope said after the Running Utes' first three home games. The natural grass was sheared off in some places, she says, but there weren't any divots or torn-up areas that are hard to restore. New grass quickly took hold, she says, thanks to the protection of the artificial base. Little hopes many more stadiums, golf courses, and other grassy spots will use SportGrass if it survives Utah's full season in good shape.



## MUSIC TO FLIERS' RINGING EARS

Ever find yourself shouting to be heard in a small plane?

Come again?

IS NOISE A PROBLEM IN SMALL PLANES?

It certainly is. But Lord Corp. of Cary, N. C., has come up with a three-pronged system to mute it. One part of the NVX Active System is a \$35,000 noise canceller, which monitors cabin noise and then generates a corresponding sound to offset it. The other two systems are vibration stillers. One resides at the engine mount, the other in the plane's skin. They transmit vibration patterns to a computer, which in turn sends commands to small actuators. These are little machines that pulsate against the vibrations, virtually eliminating them, according to Lord.

In a demonstration on a turboprop, Lord says, interior cabin noise was reduced by 80%, or 14 decibels, and vibration levels were reduced by 87%, or 18 decibels. Lord is selling its engine vibration system to Cessna Aircraft Co. for installation in next year's Citation X business jet at an undisclosed cost. Stevens Aviation Inc. has contracted to retrofit at least 50 Beech Aircraft Corp. Beech King Air turboprops with the noise-cancellation systems, but not the vibration cancellers, at a cost of \$35,000 to \$45,000 per plane.

Now if they can just silence that guy in 7-D, who's going on and on about hard-disk drives...



# ARE LIFE INSURERS BIASED —OR JUST CAREFUL?

They're under scrutiny for allegedly discriminating against some ethnic Americans and women

Last September, Lani Perkins decided that her 72-year-old mother, Pok Dong Kim, needed life insurance. Kim, a Korean-born U.S. citizen living in San Francisco, applied for a \$10,000 policy from Milwaukee-based Northwestern Mutual Life Insurance Co. To her surprise, the company rejected her a month later because she did "not meet our language requirements for the ability to understand English," according to an Oct. 11, 1994, letter. "We were shocked and upset," says Perkins. In May, Kim, Perkins, and her husband filed a lawsuit, believed to be the first of its kind, against Northwestern for national-origin discrimination.

Within a month, Northwestern got rid of its English-only rule and started providing translators for non-English-speaking applicants. "The lawsuit made us recognize there may have been insensitivities in our rule that we didn't see," says spokesman Thomas W. Towers, adding that the insurer invited Kim to reapply but hasn't heard back.

**FREE REIN.** Kim's pending lawsuit spotlights a debate over allegations of bias in the huge life-insurance industry, whose assets are estimated at \$2 trillion. Whereas lending discrimination and redlining in homeowners' and auto insurance have been under scrutiny for years, life insurance has received relatively little oversight. "Each company is free to do pretty much what it wants," says former Vermont Insurance Commissioner James H. Hunt, now at the Consumer Federation of America.

But a recent spate of lawsuits and state legislative actions suggests that life insurers might not be writing their own rules much longer. Practices being probed by state officials range from requiring applicants to speak English to denying coverage to victims of domestic



**UNINSURABLE?** Pok Dong Kim, with the Perkinses

violence. Many insurers defend these practices—which may protect against some risks—as business prerogatives that need no apology. But as ethnic Americans and women demand more clout in the marketplace, such policies increasingly clash with antibias standards. "From a purely business standpoint, there may be legitimate reasons to reject for race or gender," argues Kenney Shipley of the Florida Insurance Dept. "But we as a society have to say whether or not it's acceptable."

Hard evidence of discrimination is always difficult to substantiate, no less so when alleged by high-level executives (page 84). But a case settled in March contains some evidence that dis-

crimination may routinely tinge the sale of life insurance. The lawsuit, filed by the National Association for the Advancement of Colored People (NAACP) against the American Family Life Insurance Group in 1990, contains a transcript of a 1986 conversation between company sales manager and Milwaukee agent Rueben A. Ziehlendorf. "Very honestly, I think you want too many blacks," the manager tells Ziehlendorf. "Rube, you're going to build an agency on life insurance and blacks.... You want to sell good, solid premium-paying white people.... They want their homes." The manager was fired. "We have long had policies forbidding unlawful discrimination of any sort," says NAACP family spokesman Rick Fetherston.

The NAACP's case ended up focusing on charges of redlining in homeowners' insurance allegations of alleged discrimination in minority neighborhoods. The Madison (Wis.)-based insurer neither admitted nor denied the charges but promised in a \$14.5 million settlement to boost its business among African Americans in Milwaukee and to open offices in inner-city neighborhoods.

**AFFRONTED AUSSIE.** Now, newer forms of alleged discrimination are coming under regulators' attention. The Texas legislature outlawed English-only rules in health insurance this May after a January, 1995, report by the state's Office of Public Insurance Counsel found that some health insurers sold policies

# FREE REPORTS FROM A SELECT GROUP OF AMERICA'S FASTEST-GROWING COMPANIES

The exceptional companies listed alphabetically below want you to know more about them. Simply complete the attached coupon for **free** copies of their annual reports. Nearly every actively traded company was screened, using data provided by Standard & Poor's Compustat Services, to determine the top growth companies in America invited to appear. Invited companies ranged in size from a few giants of corporate America to emerging growth companies with sales at least \$5 million. All companies were screened for exceptional long-term sales growth, recent growth trends, size and stock price — none under \$2.00 per share.

**Only 15% of all companies on Compustat's database passed these tests and were invited to make this free offer of investor information. Thirty-four of these exceptional companies appear below.**

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# While it may be prudent for insurers to check the emergency-room records of battered spouses, is it fair?

Texas—where 20% of the population speaks Spanish—only to fluent English speakers. “Health-insurance risk has nothing to do with whether someone speaks English,” says Representative Glen Maxey (D-Tex.), the law’s sponsor.

Whether English-only rules unfairly discriminate is still subject to debate. Insurers argue that non-English speakers could sue their way out of insurance and other contracts on grounds that they don’t know English. “We’re selling a contract, and we want people to understand the contract,” says Deborah

A. Beck, Northwestern Mutual’s senior vice-president for new business.

Some companies have restricted sales even to English-speaking foreigners. In 1993, Government Employees Insurance Co. (GEICO) in Chevy Chase, Md., ended its practice of selling insurance only to U.S. citizens after an Australian filed suit, claiming he was rejected for homeowners’ insurance in 1991. The case was settled under confidential terms this June. A federal court of appeals in Richmond, Va., had held in the same case last year that laws barring bias in pri-

vate contracts covered noncitizens. GEICO contends that auto accident rates are 34% higher for foreigners than U.S. citizens. “There was a valid business reason for the policy,” says GEICO attorney Douglass Ruff. Now, “rates have to go up for everybody,” he gripes.

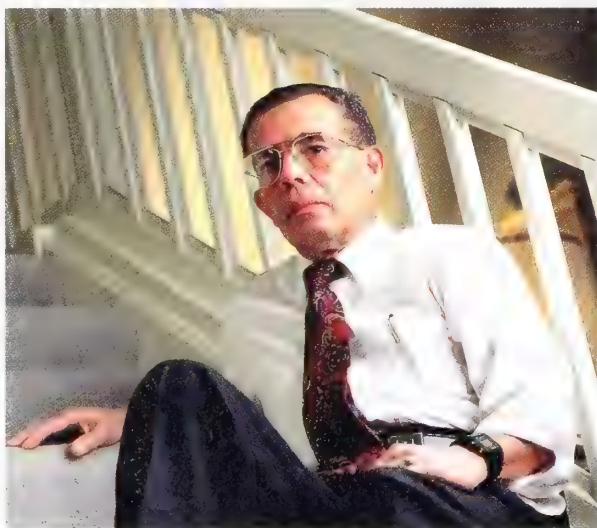
Conflicts between underwriting prerogatives and evolving social mores have also arisen in assessing risks affecting women. The National Association of Insurance Commissioners (NAIC) is working on model state legislation to prohibit insurers from denying coverage

## A DOCTOR TRIES HIS HAND AT WHISTLE-BLOWING

**M**ario S. Feliberty hadn’t been at Kemper Life Insurance Cos. for long before he began to see what he says were troubling practices at the Long Grove (Ill.) company. As its medical director from 1992 to 1994, the 55-year-old physician helped underwriters screen applicants for coverage. Feliberty says that underwriters often suggested that applicants with Hispanic or Asian surnames be denied insurance or charged higher premiums.

At the same time, Feliberty says, the underwriters recommended the approval of white applicants with similar, often routine health problems—such as fibrocystic breast conditions and elevated liver counts. “A small group of underwriters was carrying out practices that I consider very discriminatory,” he says. “They wanted to decline, postpone, or delay these applications, and I didn’t see any medical basis for that.”

**CIRCLED WORDS.** Feliberty says he met with Chief Executive John B. Scott about his concerns in January, 1993, and that Scott flatly denied the allegations. To boost his claims, Feliberty gave Scott a package of policy applications that he believed illustrated the questionable conduct.



**FELIBERTY:** *Alleges Kemper unfairly discriminates*

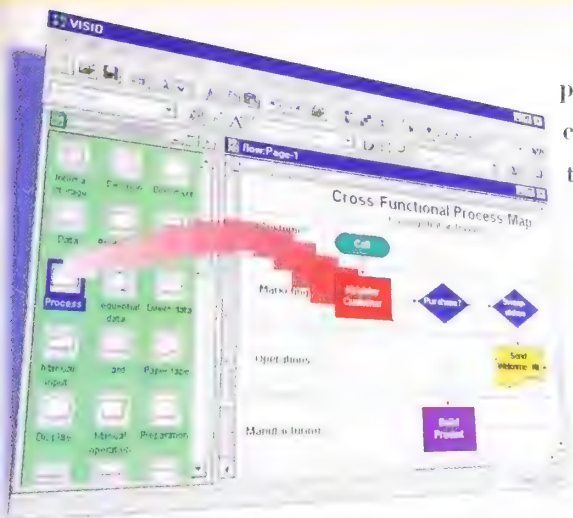
Among Feliberty’s ammunition: The words “black male” were boldly circled in applications from African Americans. Underwriters ordered special investigations to determine if certain Asian customers understood English. Managers instructed employees to scrutinize Vietnamese applicants more closely because of their supposed higher incidence of hepatitis. And Asian Indians were flagged for their alleged high rate of diabetes. Former employees confirmed that their managers told them to review applicants of certain ethnicities more carefully.

Kemper still denies Feliberty’s

claims. “We believe Kemper Life’s underwriting practices fully comply with all the law and regulations,” says company spokesman Ira Nathanson. “Any information you have received which indicates Kemper Life unfairly discriminates is wrong.” Indeed, insurance companies often say that they have actuarial studies showing higher rates of disease among certain populations. And as long as the insurance companies investigate each applicant’s health conditions, they assert that there is nothing wrong with such generalizations.

**NO INVESTIGATION.** As for Feliberty’s complaints, the Illinois Insurance Dept. has declined to investigate, in part because it didn’t see enough jilted Illinois policy applicants in the mix to justify the inquiry, according to a regulator. Complicating matters is a battle that Feliberty is waging over Kemper Life’s alleged failure to accommodate his carpal tunnel syndrome—a disability that developed in his wrists while at Kemper. In March, 1994, Kemper terminated Feliberty’s position, and the doctor is now engaged in a disabilities-discrimination lawsuit against the company. The company declines comment on Feliberty’s case.

*By Catherine Yang in Washington*



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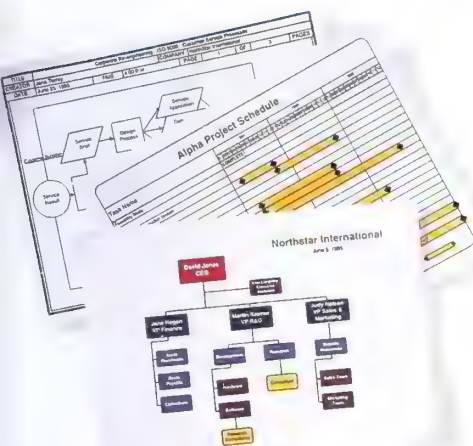
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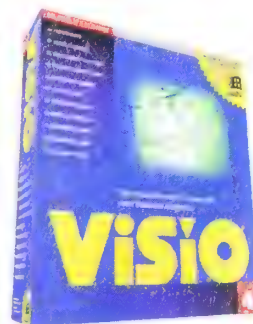
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victims of domestic violence. The state regulators say they can document, through confidential complaints, instances where insurers have turned down applicants with histories of emergency-room visits for injuries symptomatic of domestic violence. While such medical history is significant, Utah Insurance Commissioner Robert E. Wilcox says, "it's not politically acceptable today to look at it."

Similarly, the Texas legislature challenged certain medical underwriting assumptions this June when it outlawed discrimination by health insurers of women with histories of fibrocystic breast conditions. Many life-insurance companies assign higher risk to such women. But health experts say that there is little statistical evidence that this common condition is a precursor to cancer. The industry backed the bill af-

ter reaching the same conclusion, says Will Davis, a lobbyist for Texas insurance firms.

Some companies, however, have already dropped many of these seemingly faulty assumptions in order to broaden their businesses. New York-based Metropolitan Life Insurance Co. has gained ethnic customers since 1983 by hiring agents from different ethnic backgrounds and writing sales literature in languages such as Russian and Chinese. Ethnic customers now make up 25% of MetLife's business, up from 5% in 1983, says William Orton, director of client development.

But the public seems less tolerant than before of companies that still factor race or ethnicity into sales. "A lot of things are done on hunches, general understandings, and notions built into the industry that nobody questions," says William H. Lynch, the NAACP attorney who sued American Family. "The burden should be on companies to show the business necessity for a practice. As consumers start turning up the heat, insurers could discover that dropping outdated assumptions can be a boon to both sides."

*By Catherine Yang in Washington*

## Fighting Bias In Insurance

As ethnic Americans and women become more vocal consumers, insurers are facing some heat for alleged discriminatory practices. A few examples:

**MEDICAL UNDERWRITING** In June, the Texas legislature outlawed bias by health insurers against women with fibrocystic breast conditions. Many insurers had declined applicants on the basis of this common condition, which doesn't necessarily indicate cancer.

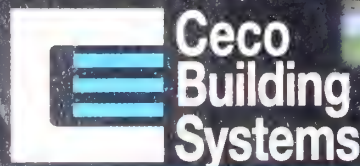
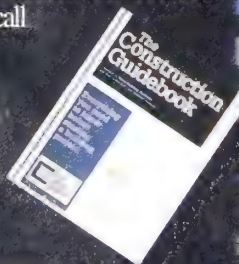
**ENGLISH ONLY** In May, a Korean-American woman sued Northwestern Mutual Life for discriminating against her on the basis of national origin when it declined her application because she didn't speak English. Northwestern has since ended its English-only rule.

**DOMESTIC VIOLENCE** After a wave of consumer complaints, the National Association of Insurance Commissioners is working on a model state law to prohibit the denial of insurance to victims of domestic violence.

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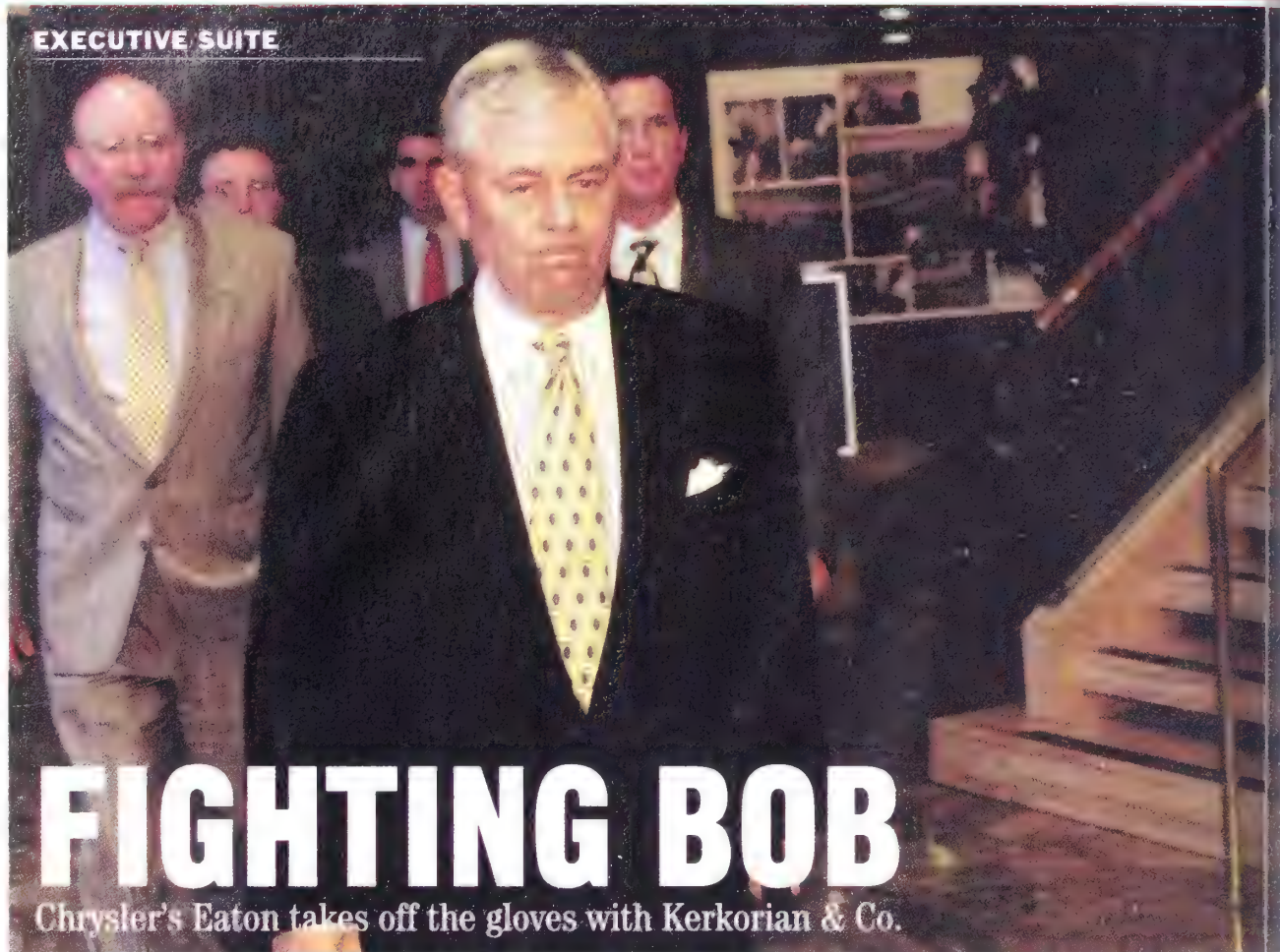
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## EXECUTIVE SUITE



# FIGHTING BOB

Chrysler's Eaton takes off the gloves with Kerkorian & Co.

**W**ith Chrysler Corp.'s Gulfstream II climbing to 43,000 feet, Robert J. Eaton can finally sit back and relax. He loosens his tie, unbuttons his collar, and grabs a turkey sandwich. "I think it's been a good day," he says. He's heading back to Detroit on Oct. 3 from New York, where he has just delivered the most important speech of his life. After months of holding his fire, Chrysler's chairman had finally unloaded on his nemesis, Las Vegas billionaire Kirk Kerkorian, in an address to the Council of Institutional Investors.

Now, as he settles into the leather seat of the company jet, Eaton, 55, breaks into a rare diatribe. Kerkorian, he rails, isn't fit to run Chrysler. And Eaton isn't going to let him. Investors, he says, "don't want a Las Vegas gambler running Chrysler."

It's not just business anymore: Now it's personal. By all rights, Bob Eaton should be savoring triumph. Since leaping from General Motors Corp. to Chrysler in 1992, he has been presiding over the most successful period in the No. 3 carmaker's checkered history. Sales are soaring, profits have hit a record, and

market share is on the mend. But instead of reveling, Eaton is fighting for his professional life. As Kerkorian presses his campaign for control of Chrysler, he and his aides are making Eaton and his track record, management style, and strategic vision the central issue. In conversations with reporters and with the powerful institutional investors who will ultimately decide the battle's outcome, they are tarring Eaton as a man more lucky than smart.

The fight became a grudge match after Eaton embarrassed his largest investor by quashing Kerkorian's \$20.5 billion takeover bid last spring. Since then, Kerkorian has hired more firepower: a proxy solicitation firm, investment bankers Wasserstein Perella & Co., Washington-based shareholder activist Ralph Whitworth, and Jerome B. York, the former Chrysler chief financial officer

**STEADFAST:**  
*Eaton  
defends his  
track record*

who had become 11th-ranked cost-cutter. Kerkorian's troops are masters for a proxy fight.

Far from giving Eaton any credit for Chrysler's current success, Kerkorian & Co. have a litany of complaints about him: He's a blithering indecisive manager. He has failed to hammer home to subordinates the need to improve Chrysler's spotty quality. His insistence on amassing a \$7.5 billion nest egg to carry the auto maker through the next recession is ridiculously overcautious, as is his reluctance to increase the company's debt. And he has been way too timid in pushing into the expanding world markets that promise the greatest future growth.

The ad hominem nature of the Kerkorian camp's escalating campaign put Eaton in an uncomfortable spot. In



"If they thought I was going to roll over and let them take advantage of this company, they misjudged me"



as-bred engineer is an almost painfully unassuming man who ritually uses the pronoun "I," preferring to credit with his management team. He has been mum on Kerkorian and relatively mild in his public comments on the investor's charges—until now. Kerkorian has absolutely destroyed the companies: Columbia Pictures and UA," Eaton says. "It would be a good idea to let him and his group do it at Chrysler. If they thought I was going to roll over and let them take advantage of this company, they absolutely judged me."

Eaton is vehement in defending his strategies for Chrysler. That big cash infusion he says, is essential to maintain Chrysler's capital spending to upgrade facilities and develop snazzy vehicles—and keep profits high—when the inevitable downturn comes. The cash and strong balance sheet are necessary to finance global expansion. In a reversal of his earlier reluctance to establish new assembly plants, Eaton says that he's contemplating a half-dozen deals to set up major new operations in places as China, India, South America. And while Chrysler's quality still lags behind most of its competitors', Eaton notes that he's already making big strides to better vehicle quality, as measured by the company's warranty improved 26% during the last three years.

**WOODEN.** In many ways, Eaton is the antithesis of his predecessor, Lee A. Iacocca, the washbuckling ex-chairman helping Kerkorian wage his campaign. While Iacocca, for a time, idolized by Wall Street, the press, and the public, the company's board was many in his management chafed under his high-handed ways. By contrast, Eaton comes across as a bit more in public, contributing the impression that he's informal and bureaucratic. But others know a different Bob Eaton: a flexible, forceful man—who is willing to listen and learn. They describe him with formidable people who has forged a consensus group of brilliant managers into a cohesive team. "I think people realize that he is a fantastic leader," Chrysler director Joseph J. LaFollette Jr. "He has ener-

gized the talent at that company to be more than the sum of its parts. His style is just right." Iacocca declined to be interviewed for this story.

And while Eaton's low-key persona may not wow Kerkorian or Wall Street, a swaggering superstar could well be the last thing Chrysler needs right now. To his boosters, Eaton represents the new breed of boss at the Big Three: the prudent shepherd of corporate resources for long-term prosperity. If he's a little bland, that's a small price to pay for blunting Detroit's brutal boom-bust cycles, with their devastating layoffs, plant closings, oceans of red ink, and suspended dividends. Even big investors who privately call Eaton uninspiring are reassured by his steady influ-

ence on Chrysler, which has had two close brushes with bankruptcy in 20 years. "I'm more scared of inspiring CEOs," says one shareholder. "I just want to see the auto companies run profitably in a very boring way."

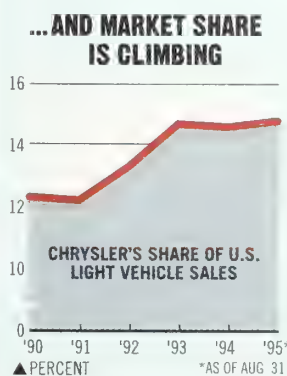
By most measures, Eaton is the right man to do just that. He kept GM's European turnaround on course with a raft of new models and stringent cost-cutting discipline. When he ran GM's mammoth technical staff, he had to mesh the company's feuding fiefdoms of designers and engineers. And at Chrysler, Eaton did something that many thought impossible: He formed a solid alliance with Robert A. Lutz, Chrysler's charismatic president, who never hid his disappointment at losing out on the top job when Iacocca finally retired. Lutz says he quickly felt an affinity with his new boss: "Finally, I had a superior here I could respect."

**LINE OF DEFENSE.** Eaton's first line of defense against Kerkorian is just how well Chrysler is doing these days. The company is riding high: Profits last year hit a record \$3.7 billion on sales of \$52.2 billion. The car-maker's pension fund—\$4.4 billion short in 1991—was fully funded for the first time since the 1950s. Those two accomplishments prompted Standard & Poor's to give Chrysler its first A credit rating since 1969 and remove the stigma and higher costs of the junk-bond rating that Chrysler carried less than two years ago. "Look at my record, and compare it to Kerkorian's, Iacocca's, and York's," Eaton says. "Chrysler has produced a greater return on investment than any company they've ever been associated with."

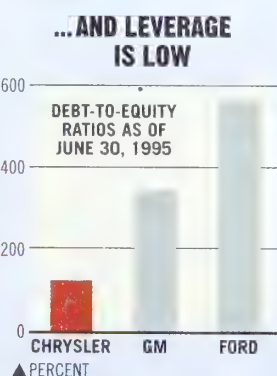
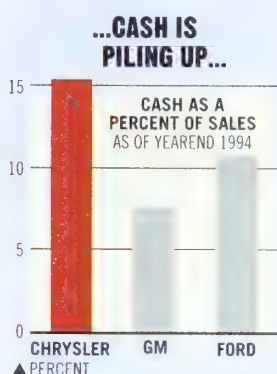
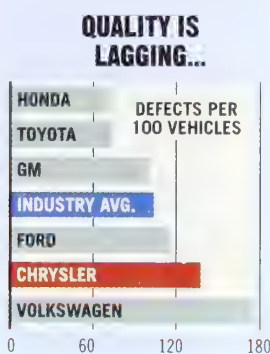
The financial rebound is driven by some of the most exciting cars and trucks coming out of Detroit. While Chrysler's lineup suffers from uneven quality, there's no doubt which auto maker sets the pace for stylish design. Vehicles such as the Jeep Grand Cherokee, the Dodge Ram pickup truck, the LH family sedans, the Neon small car, and the minivans have boosted Chrysler's share of U.S. light-vehicle sales 2.5 points since 1990, to 14.8%. Thanks to aggressive cost-cutting in the early 1990s, Chrysler claims the title of the world's lowest-cost auto producer.

It's true that the turnaround

## Chrysler Has Come Roaring Back...



## ...But Kerkorian Sees Signs Of Weakness



DATA: BLOOMBERG FINANCIAL MARKETS, COMPANY REPORTS, WARD'S AUTOMOTIVE REPORTS, J.D. POWER & ASSOC., BUSINESS WEEK



# The Corporation

was well under way before Eaton set foot in Chrysler's Highland Park (Mich.) headquarters in March, 1992. Lutz, a charismatic former Marine fighter pilot, was the one who revamped Chrysler's engineering ranks into nimble, cross-functional teams that designed an all-new roster of cars and trucks cheaply and quickly. And it was York who squeezed \$4 billion out of Chrysler's annual costs before leaving to become CFO at IBM in 1993. "Eaton was probably the luckiest businessman in America," says one former Chrysler executive. "He walked into a situation that was about perfect." It's a view that has some resonance among Chrysler's institutional shareholders. "If Bob Eaton has left his stamp on Chrysler, I've yet to see it," grumbles one. "A lot of investors are still there because of Bob Lutz."

Eaton sharply contests the view that he's just the happy beneficiary of a rising tide. "When I came to Chrysler, it did not have a long-term strategy. It did not have a mission," he says. It does now, he adds—and for the first time, he's willing to take the credit. "Yes, I'm the guy behind it. I'm the guy pushing for cultural change." Vice-Chairman Thomas G. Donomme agrees: "Before Bob, we had never tried to fundamentally change how we work together. He was the teacher. He was the catalyst."

Eaton's aim is to make Chrysler a more dependable, predictable place run by a cohesive team of managers. He vows an end to Chrysler's history of crises and cliffhangers. "Every previous chairman of Chrysler since Walter P. himself has had the opportunity to make history by presiding over a dramatic Chrysler turnaround," he told the Council of Institutional Investors. "I [want] to be the first chairman never to lead a Chrysler comeback."

Hardly flashy. But Eaton likes to play the Kansas mechanic, making small but continuous improvements throughout

the organization. That's a hallmark of the auto company that Eaton considers the world's best, Toyota Motor Corp. He has borrowed heavily from the Toyota handbook, keeping financing cautious, aiming for constant gains in quality and productivity, and giving employees more say in the workplace.

That philosophy isn't so far from the conservative values instilled in Eaton

City *Daily Traveler* for 35¢ a day. two years, he had saved \$10 to buy a rattletrap black 1932 Ford, which promptly took apart. "I wanted to know how it worked, and I was absolutely sure that I could make it better somehow," he recalls. Once he got the lumpy back together, Eaton was hitting down back roads long before he was old enough for a driver's license.

## VROOM!: Eaton at N Celebrity Challenge



**ROBERT J. EATON**

**FEB. 13, 1940** Born in Buena Vista, Colo.

**1963** Earned B.S. in mechanical engineering at University of Kansas; joined GM's Chevrolet Motor Div. as trainee.

**1963-76** Promoted through a series of jobs on Chevy and corporate engineering staffs. Worked briefly for John DeLorean, served as chief engineer for the X-car.

**1976** Named chief engineer for GM car programs.

**1979-82** Worked for GM's Oldsmobile Div. as assistant chief engineer, then director of quality and reliability.

**1982-88** As chief of GM's advanced engineering staff, led technical team for federal X-car recall trial; headed technical staffs.

**1988** Named president of General Motors Europe.

**MARCH, 1992** Hired by Chrysler as Lee Iacocca's successor, named vice-chairman and chief operating officer.

**JANUARY, 1993** Became Chrysler chairman and chief executive.

during his boyhood in rural Arkansas City, Kan. His father, Eugene, was a brakeman and conductor for the Santa Fe Railroad, and his mother, Mildred, ran a beauty shop in the basement of their home. "Bob worked for absolutely everything he got," recalls childhood friend Bob Foster, who now runs a furniture store there.

Dreaming of his own car—at age 9—Eaton began delivering the Arkansas

The paper route and other jobs, such as selling packages at Montgomery Ward, for cash for parts to run the series of old cars and motorbikes Eaton acquired before collecting 15 cars and 12 motorcycles in all. To pay for college, Eaton worked the wheat harvest, picked strawberries, recruited classmates from the University of Kansas to work in Oregon pea canneries where he became superintendent. Eaton was fascinated by machinery and processes and was always interested in how everything worked. "How you canned how you ran a combine or a Caterpillar," says Stephen Ross, a high school classmate and Kappa Sigma fraternity brother who now works as an insurance agent in his hometown.

Eaton married his college sweetheart, Carol Drake, from Burlington, Kan., in 1964. The couple moved to Des Moines where Eaton had landed a job as an engineering trainee at the Chevrolet Div. Co. taught grade school, while Bob began working his way up GM's engineering ranks. The couple raised two sons, now 23 and a marketing manager, and Matthew, 21, a student at Boston University.

Eaton's career quickly moved to high gear. Just 2½ years out of college as a research engineer, Eaton was subpoenaed by the plaintiff in a big civil liability case against GM alleging that



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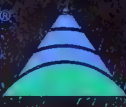


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# The Corporation

Chevrolet Corvair was prone to roll over. "I was on the witness stand for eight days," Eaton recalls now. "They attacked anything and everything." GM won the case.

Eaton moved onto the GM fast track as chief engineer for the X-car, GM's first front-wheel-drive auto. He helped lead the effort, during the second Arab oil embargo, to rush out the family of fuel-efficient compact cars, which included the Chevy Citation and Buick Skylark. "It was a real trailblazer," says former GM President Lloyd Reuss. "It was a major change in the way the American auto industry built cars."

**GREAT TIMING.** Not everyone was so enthralled with the X-cars. Quality was shoddy, and the rear brakes tended to lock up. By 1983, the Justice Dept. filed suit to force GM to recall 1.1 million of the cars for the alleged brake defect. Eaton headed the technical team, devising elaborate tests to compare the X-car with hundreds of other models and rallying a group of engineers, economists, and lawyers to keep plugging away through a 30-month legal process. Once again, Eaton held his own on the witness stand, while demonstrating the feistiness he's newly displaying in his fight with Kerkorian. Eaton was "a handful to cross-examine, very combative. He wouldn't just answer your question—he would argue with you," says Larry Moloney, the government's lead prosecutor on the case.



**YORK** Chrysler's ex-CFO works for Kerkorian

"He probably hasn't changed much."

GM won the X-car case in 1987, and Eaton was soon off to Zurich to run the company's European operations. It was another case of great timing. He arrived just as the financial overhaul and consolidation of GM's German and British units was beginning to click, and Europe's economy was rebounding. Eaton rode the wave as GM Europe contributed \$1.7 billion to the company coffers in 1991, even as its North American operations were losing \$7.9 billion.

To his critics, Eaton was sometimes slow to seize new opportunities. He initially resisted subordinates' urgings to jump into Eastern Europe by building a GM plant at Eisenach in the former East Germany. He finally agreed—and Eisenach has become the most productive auto plant in Europe, according to a re-



**KERKORIAN** He's massing troops for a proxy fight

cent independent study. But his boss at the time, GM Chairman John F. Smith, disagrees that Eaton was overcautious. "He was very bold and aggressive in developing our position for eastern Europe," Smith says.

Eaton's friends at GM further point to

his speedy acquisition of Saab as proof that he can act quickly and decisively. Eaton had been trying to buy a 20% interest in Jaguar PLC when Ford Motor Co. swooped in with a \$2.5 billion bid for the whole company. Instead of trying to outbid Ford, Eaton cast an eye on Saab. "He immediately saw opportunities there that none of us had seen before," says Tom Mason, who headed Europe's marketing at the time. In a three-week blitz, Eaton pulled off a surprise \$500 million deal, giving GM an upscale brand to sell alongside its mainstream market Opel line in Europe.

**"BOXY CARS."** When Chrysler direct came courting Eaton, the move from GM Europe looked like a leap into the unknown. "In 1992, like most people in the industry, when I thought of Chrysler, I thought about bankruptcy and boxy cars," Eaton says. But when he showed him where Chrysler was heading—the stylish new cars and streamlined organization—he jumped. The board wanted Eaton because they were ready for a change. "We wanted a different style," says Director Robert Lanigan. "Bob is a modern-day manager. He doesn't need a round of applause when he comes to work every day."

Nonetheless, the atmosphere at Chrysler's fifth-floor executive offices in Highland Park was tense when Eaton arrived on Mar. 16, 1992. The board had agreed to let Iacocca stay on as chairman until the end of the year, with Eaton serving as vice-chairman until then. That did little to mollify Iacocca, who was bitter that the directors were forcing him to retire. If anyone was in a blacker mood, it was Lutz, who fumed about being passed over. Inpenchant for butting heads with Iacocca while championing daring styling and sporty performance had cost him the top job. And Chrysler's senior executives wondered openly how button-down Bob Eaton would fare in the rough-and-tumble environment. Says Vice-Chairman Denomme: "He had officers here looking at each other

## 1996 CARAVAN

A new generation of minivans should help Chrysler maintain its market-share momentum



## 1996 CIRRUS

In the latest J.D. Power survey, it still ranks in the bottom-fourth among all cars sold in the U.S.

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"The SAS System is the fuel behind those forecasts...our software of choice for analyzing sales, economic, and auto industry data and then reporting what we've learned," adds Rosenthal. "Before the SAS System, much of the forecasting was done by hand. To make our forecasts credible, we had to have a credible system. One that made it easy to build applications and put them to work across our computing environments. We've got minis, Macs, desktop publishing, and a lot of spreadsheets. The SAS System fits the way we do business."

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Now that the forecasting model is up and running, Rosenthal and his staff are using the SAS System to build an interactive database. "The Power Information Network will allow an auto dealer or manufacturer to go online and get market information," Rosenthal explains. "When released,

subscribers will be able to select from a long menu of reports and data. The versatility of the SAS System is crucial in developing the reports."

"The bottom line is this: applications are being developed with the SAS System that will deliver the most up-to-date information to those who make decisions for the automotive industry," says Rosenthal. "If manufacturers and dealers can get their hands on accurate market information and predictions, they have a much better chance of meeting customers' needs down the road."

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**Executive Summary**



g, 'A GM guy? You've got to be  
ing.'

curately reading the mood, Eaton  
rately kept a low profile during  
ne months as CEO-in-waiting. He  
d plants, roamed the labs at the  
der Technology Center, and sat in  
etings more as observer than par-  
nt. He methodically studied the  
ization—to the point of walking a  
budget request through the bu-  
racy to see how the process could  
reamlined. Above all, Eaton  
ed how Chrysler was run—then  
out to change it.

ping his list was uniting Chrysler's  
ng camps. Under Iacocca, senior  
yers from marketing, sales, and fi-  
were often pitted against the engi-

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d at the lobby. As managers ar-  
Eaton and Lutz parked their cars  
oted their luggage. Dressed in  
s and wearing half-moon reading  
s, Eaton led give-and-take ses-  
on empowering employees, foster-  
amwork, setting goals, and re-  
ng achievers. Graduates later ran  
ns for their subordinates. The cul-  
hock was enormous. "In the old  
only one person would talk," says  
"Dissenting voices were not easi-  
erated and could be considered  
reer-enhancing."

on and Lutz quickly formed a  
—and they plan to stay one. De-  
praise from York, Lutz says he  
never work for a Kerkorian-con-  
Chrysler. And Chrysler's board is  
tted to keeping Lutz on board af-  
reaches mandatory retirement

age of 65 in February, 1997. "Bob Lutz  
makes a hell of a contribution to this  
company, and I intend to see he keeps  
doing that," Eaton says.

Not everyone appreciated the new  
Eaton regimen, though. "There was sort  
of a harshness to it," says one former  
Chrysler official. "The feeling was you  
will become a team player, and the  
stragglers will be shot." Eaton doesn't  
disagree: "If people can't change, then  
you're going to have to get some new  
people."

To managers who embrace his em-  
phasis on teamwork, Eaton is collabor-  
ative and flexible. Instead of leaving  
top executives to speculate on what goes  
on in Chrysler's sacrosanct boardroom,  
Eaton briefs them afterward. And unlike



**LUTZ IN HIS JET:** "A lot of investors are still there because of Bob Lutz"

Iacocca, Eaton suggests changes rather  
than orders them. Manufacturing chief  
Dennis Pawley recalls how Eaton pro-  
posed reducing automation in a plant's  
body shop but deferred to Pawley's reas-  
oning that extensive manual welding  
could hurt quality levels. Says Pawley:  
"Bob never second-guesses you."

**STRATEGIC ROADMAP.** Eaton is willing  
to heed dissenting voices on even the  
most sensitive decisions. Earlier this  
year, for example, Chrysler was be-  
sieged with lawsuits from accidents in  
which the rear gate latches of minivans  
flew open in collisions, ejecting passen-  
gers. Federal regulators were threat-  
ening a recall, and tabloid TV was trash-  
ing the image of the quintessential  
family vehicle.

Eaton attacked the problem the same  
way he did the X-car case at General

Motors. After poring over minivan  
crash-test data, the latch's design spec-  
ifications, and the accident rates of com-  
parative vehicles, both he and Lutz  
came to the same conclusion: The latch-  
es were safe, and Chrysler should fight  
back. The rest of Chrysler's top brass  
opposed the idea. They argued that dur-  
ing the inevitably long battle to prove  
the latch's safety, Chrysler's reputation  
could be irreparably harmed by the pub-  
licity. In March, Eaton agreed to re-  
place the latches on 4 million minivans  
at a cost of \$115 million.

Eaton rarely strays from his overall  
strategic roadmap for Chrysler, though.  
He steadfastly refuses to consider any  
acquisition that would diversify Chrysler  
beyond autos—such as Iacocca's acqui-

sition of Gulfstream  
Aerospace Corp. In-  
stead, Eaton's plan is  
to funnel Chrysler's  
record profits into  
new equipment for  
its aged plants. And  
he has earmarked  
\$23 billion for devel-  
oping new vehicles in  
the next five years.

And when it  
comes to how much  
money the auto mak-  
er needs to weather  
the next recession,  
Eaton is holding firm.  
For Jerry York,  
Eaton's reluctance  
to pump some of  
Chrysler's \$6.9 billion  
cash hoard into big-  
ger dividends or a  
stock buyback pro-  
gram is evidence that  
Eaton is too cautious.

"They're saying they are betting on a  
bone-crushing recession in combination  
with Chrysler becoming noninvestment  
grade," York scoffs. "But it's not 1990  
anymore."

Eaton won't budge. And when he  
makes up his mind, even his closest as-  
sociates admit he can be mighty stub-  
born. "Bob Eaton knows exactly what  
he wants," says Lutz. "This guy is not a  
wimp." Indeed, Eaton's belated flashes  
of temper belie that famous mild man-  
ner and reveal his combative streak.  
"The meek may inherit the earth, but  
they don't go far in business," he says.  
Eaton has gone far—and he's making  
it clear that he intends to wage a fierce  
fight to stay there.

*By Bill Vlasic and Kathleen Kerwin,  
with Keith Naughton and David  
Woodruff, in Detroit*



## SWEATSHOPS

# LOOK WHO'S SWEATING NOW

How Robert Reich is turning up the heat on retailers

**A**fter federal agents raided an El Monte (Calif.) sweatshop last August that had enslaved 72 Thai immigrants, Labor Secretary Robert B. Reich wasted no time. He ran straight to the media with the names of several large retailers whose names had been found on boxes in the dingy shop. Angry and embarrassed, Sears, Montgomery Ward, and Dayton Hudson agreed to meet Reich in New York in mid-September to discuss ways to combat the use of sweatshops. Even though the chains aren't liable if they unknowingly sell illegally made goods, they promised to adopt a statement of principles calling on their suppliers to adhere to federal labor laws. Retailers fervently hoped that this would end the public-relations debacle and get that pesky Reich off their backs.

No such luck. In recent weeks, Reich has drawn up plans for a media blitz against retailers. His aim: to get stores to crack down on sweatshops by policing the 20,000 tiny U.S. garment makers that supply the half of the country's clothing that isn't imported. He fired the latest broadside during an Oct. 2 appearance on *The Phil Donahue Show*, where he showed a videotape of the Thai workers who had been held behind barbed wire and paid less than \$1 an hour. The largely blue-collar audience cheered when one of them said: "Nobody can live on even \$4 and change an hour. We're all being exploited."

Reich isn't stopping there. He's planning more sweatshop raids and promises to name more stores that sell sweatshop-made goods in a full-scale campaign beginning the week after Thanksgiving. That's the start of the four-week Christmas buying season, when stores rake in 20% of their annual sales. Although it's unclear just how responsive consumers will be, "Reich could hurt the industry," warns Robert C. Blattberg, director of the Center for Retail Management at Northwestern Uni-

versity. Even "a small percentage change in sales can mean a big change in profits."

There's not much doubt that garment sweatshops, once considered a turn-of-the-century problem, have surfaced in a big way under the pressures of a global economy. It's partly because of the way the apparel industry works. At the top, large retailers sell clothes to the public and negotiate prices with large manufacturers. Manufacturers, from Guess jeans to Ralph Lauren, design garments and rely on some 20,000 subcontractors to sew the clothes. While the industry employs 800,000 people in the U.S., most shops are tiny, with 5 to 50 workers, and they go in and out of business at the drop of a pin. The workforce: mostly female immigrants from

### BULLY PULPIT

Reich is calling for retailers to mount their own random checks of subcontractors

Latin America and Asia. They earn an average of \$7.50 an hour—just over the federal poverty level.

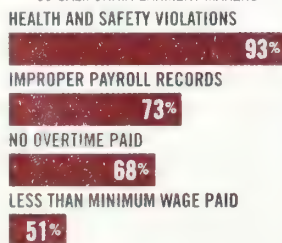
The apparel industry has been under fierce pressure from imports in the past few years, largely because the work is so labor-intensive. The competition has driven down wages in the U.S. and fostered the spread of sweatshops. A 1989 report by the General Accounting Office found that some two-thirds of the 7,000 garment shops in New York City were sweatshops. Last year, a Labor Dept. spot check of 69 garment shops in Southern California found that 93% had health and safety violations (chart). **BUYING POWER.** The Labor Dept. has had a tough time keeping up. Cutbacks by Presidents Reagan and Bush slashed the number of investigators to 816 from 911 in 1989. And congressional Republicans' current budget-cutting efforts have targeted an additional 12% reduction for investigators, who must police all 6.5 million employers covered by federal labor laws.

Now Reich wants the retail industry to take up the enforcement slack. Last week he mounted a series of attacks against garment manufacturers, invoking a little-used 50-year-old law to hold them liable for their suppliers.



### SWEATSHOPS ARE WIDESPREAD...

A SNAPSHOT OF THE INDUSTRY  
BASED ON A 1994 RANDOM CHECK OF  
69 CALIFORNIA GARMENT MAKERS



### ...YET INSPECTORS ARE SCARCE

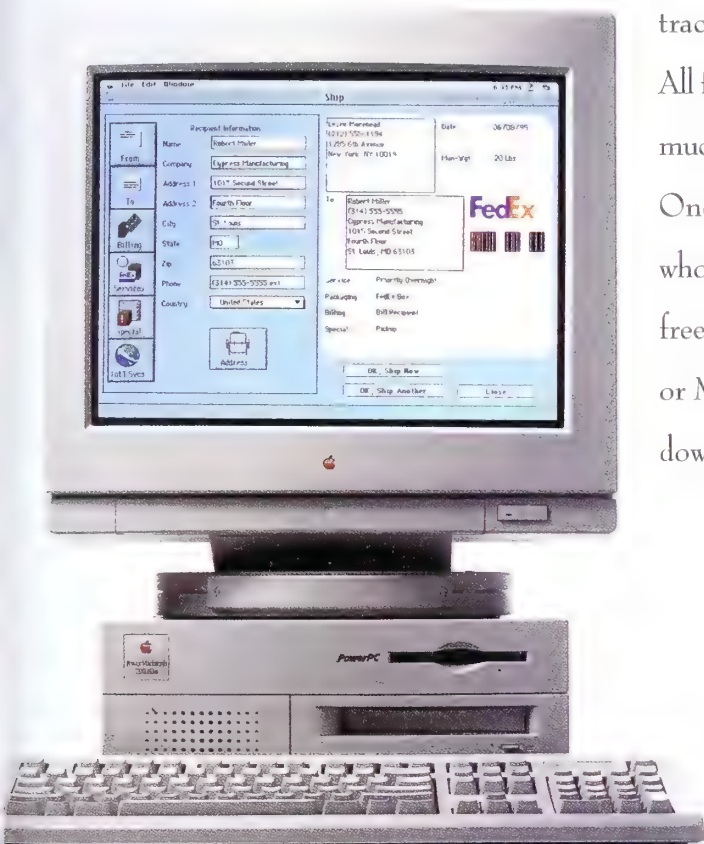


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# 1984



Sarajevo, Olympics

# 1995



Sarajevo, Battleground

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## The Workplace

illegal actions. The law doesn't cover retailers, however.

So the Labor Secretary is turning to public pressure. His goal is to get retailers to use their immense buying power to make sure that subcontractors comply with labor laws. Mainly, he wants them to mount spot checks of their own. Retailers should hire inspectors to visit shops randomly and without warning, he says. "We need to enlist retailers as adjunct policemen," says Reich. "At a time when business says to government, 'Get off our back. We can do it ourselves,' we're giving them the opportunity."

The retailers say such demands are unfair. The logistics would be enormous,

Retailers also argue that their contracts don't say anything about spot checks. "We don't have the legal authority or the manpower to do this," says Tracy Mullin, director of the National Retail Federation, a trade group. "The Labor Dept. is trying to get us to do their work for them."

**LEVERAGE.** Reich retorts that retailers are just ducking the issue. They can afford to hire a few inspectors with legal expertise, he says. The giant companies also have plenty of leverage to force both manufacturers and minuscule shops to accept new contracts allowing random spot checks. And while the task may be daunting, any added enforcement is better than doing nothing.

## Montgomery Ward



for one thing. A large department store such as Sears, Roebuck & Co. has up to 10,000 direct suppliers, which in turn farm work out to even more subcontractors. Nor do stores have the expertise to detect violations in the government's "very complex" wage and hour laws, says the general counsel at one large retailer. "We can go into a location, but that doesn't mean we would know what we're looking for," he says.

Just making the connections between supplier and retailer isn't always easy. Sears and Mervyn's, a division of Minneapolis-based Dayton Hudson Corp., which were identified as receiving goods from the El Monte shop, still haven't been able to confirm the charge after two months of investigating. Montgomery Ward did confirm a connection and has filed a federal lawsuit against its supplier, New Boys Inc., which subcontracted with El Monte.

### P. R. PROBLEM

Montgomery Ward was among the big retail chains embarrassed by ties to slave labor

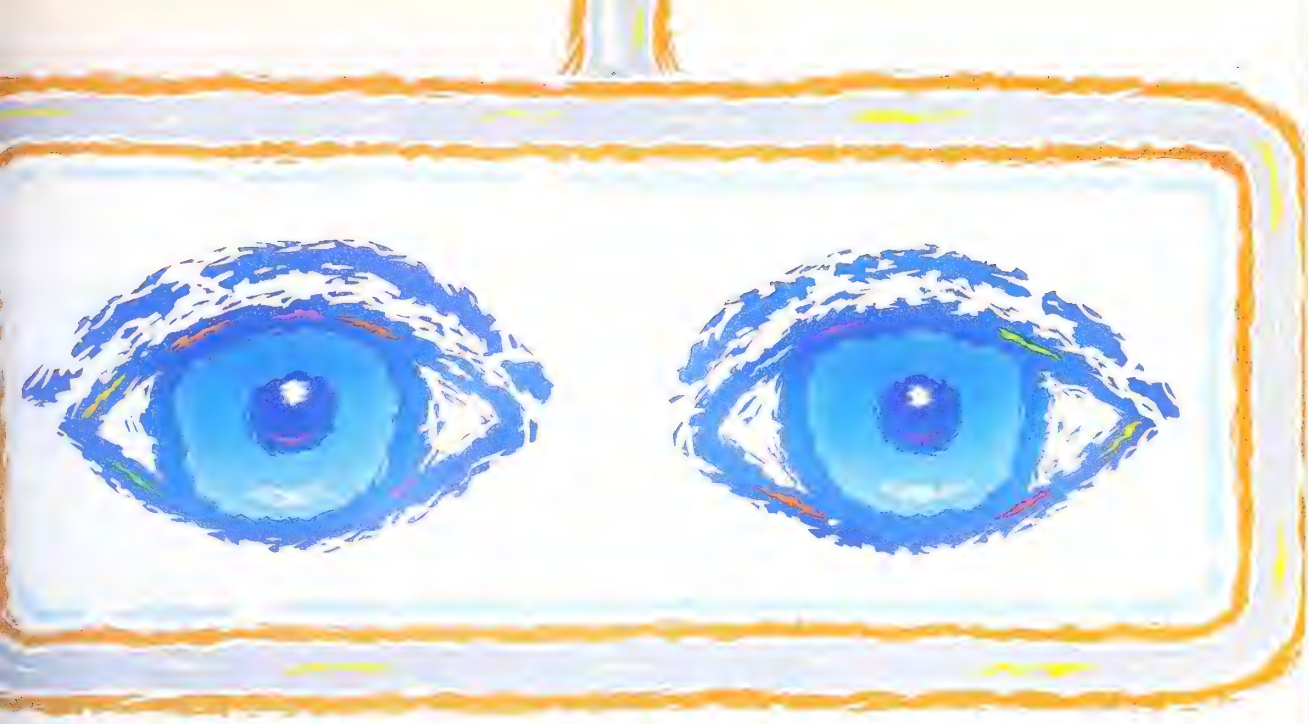
the Labor Dept.'s resource

dwindle. Still, it's possible that Reich's campaign won't drive price-conscious consumers, says Northwestern marketing professor Mohan Sawhney. After all, union campaigns against companies

that make sweatshop goods here and abroad have had relatively little impact.

But image-sensitive retailers are not want to run the risk. They're suffering through a fourth tough year of lackluster apparel sales and need a home run at yearend. "We didn't know it wasn't much of a rallying cry, concealing Robert L. Mettler, Sears' president of apparel, who wants fellow retailers to find ways to address the issue. Retailers aren't directly responsible for sweatshops. But if Reich has his way, they'll have a lot more responsibility in the future.

By Susan Chandler in Chicago



## A Company Wanted Its Truckers To Drive Safely.

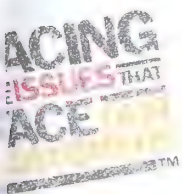
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# BIG TROUBLE IN THE BIG EASY

Developer Chris Hemmeter makes a bad bet on riverboat gambling in New Orleans

It was quick, slick, and quintessential Chris Hemmeter. In the fall of 1991, Daniel P. Robinowitz, a Dallas-based developer and New Orleans gambling maven, was set to sign a deal with Mirage Resorts Inc. to build a casino if, and when, one was approved in New Orleans. On the eve of the signing, Hemmeter, eager to get a foothold in the nascent Louisiana gaming market, swooped into Dallas aboard his private jet to make Robinowitz a generous counteroffer. Within hours, Christopher B. Hemmeter was in and Mirage was out.

At the time, it seemed like a major coup for the 55-year-old Hemmeter, a flamboyant but soft-spoken developer of luxury resort hotels. He had amassed a \$200 million-plus fortune building Disney-style megaresorts in Hawaii in the 1970s and 1980s. By 1991, he had concluded that the Big Easy would be the next great gambling haven. Armed with Robinowitz' political contacts and \$140 million in junk-bond financing, he launched his \$223 million River City casino project last March.

**BETTING THE RANCH.** But just nine weeks later, the project ran out of money, and shortly afterward creditors threw it into bankruptcy. In August, Hemmeter was forced out as chief executive of Denver-based Hemmeter Enterprises Inc. and Resort Income Investors, a publicly traded real estate investment trust. He now faces investor lawsuits alleging financial irregularities. "I have to go back to the beginning and start over again," he says with a sigh.



**STARTING OVER:** Hemmeter plans to bank again on resorts

How did Hemmeter, who had expected his New Orleans project to be a slam dunk, manage to blow it? Hemmeter dismisses the debacle as nothing more than his overly optimistic outlook for the New Orleans gambling market, a mistake which he insists was shared by many developers and investors, including his own. "Everyone misread the market," says Timothy Ryan, dean of the business school at the University of New Orleans.

But others who know Hemmeter well say he should bear much of the blame. Hemmeter, they say, is a stubborn, impractical man with grand visions but modest managerial and financial savvy. Yet he seemed bent on making each new project more grandiose than the previous one. Apparently convinced that

he couldn't lose, Hemmeter bet the ranch—some \$180 million—on the New Orleans market. And by the time he arrived there in 1992, Diane J. Plott, his financial and operations manager, had played a key role in his ventures.

Although Hemmeter, in growing up sometimes lived hand-to-mouth, pragmatism was never one of his strong suits. His five Hawaiian resort hotels, which began building in 1970, included such lavish features as waterfalls, dolphins in swimming pools. Each project was more opulent than the last. Hemmeter and his investors then sold the reaping huge profits.

His fortunes began turning in the early 1990s. One cause was Diane Plott's retirement in 1991, though

she remained on the board of directors. "To a great degree, she was responsible for Hemmeter's success," says Robert Fishman, a former executive with Hemmeter's aviation subsidiary and managing director of the city of Honolulu. "She was a CEO-type individual which complemented Chris, who was the visionary. She had a sixth sense about how to make deals work, which allowed Hemmeter to be creative."

**DOOMED.** After a few efforts to launch additional resorts failed, Hemmeter turned to gambling. In 1992, he opened two casinos in Colorado. But before they were running profitably, Hemmeter moved on to New Orleans. He wanted to go it alone. Big players like Harrah's, Horseshoe, and Bally's also eyed the Big Easy. Hemmeter originally planned to build

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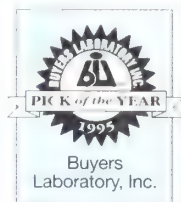
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a mega land-based casino. But even with Robinowitz' help, Hemmeter lost that project to Harrah's, settling for a one-third interest.

Still convinced he would hit the mother lode, he snagged a license in 1993 to operate a riverboat casino. His Hemmeter Enterprises' subsidiary, Grand Palais Riverboat, and a subsidiary of Atlantic City-based Capital Gaming International Inc. formed a 50-50 joint venture to operate a two-boat casino complex, called River City, near downtown New Orleans.

In December 1993, Hemmeter Enterprises sold \$140 million worth of junk bonds underwritten by Salomon Brothers Inc. to finance its half of the project. The projected cash flow would not only fund the junk but pay off debt on its two Colorado casinos. By now, Hemmeter had accumulated more than \$200 million in new debt, some of it personally guaranteed by him.

But River City was probably doomed from the start. For one thing, it was located beyond walking distance from most of the city's hotels. And it was in a seedy part of town with warehouses, manufacturing plants, and a low-income housing project. Hemmeter, whose company built the project, pressed ahead with characteristic flourishes, such as the creation of a mythical Louisiana river town in the casino boat terminal and \$250,000 faux oak trees. Within months, costs ballooned from \$196.3 million to \$223 million, creating a cash crunch from the start. "If they had been on budget, they might be around today," says analyst Larry Klatzkin of Donaldson, Lufkin & Jenrette Securities Corp. "But they didn't have any money left for day-to-day operations."

When the two riverboats finally began operating in late March and early April, they faced fierce competition in a saturated market that has failed to attract large numbers of gamblers, who tend to prefer Vegas and Atlantic City. According to Hemmeter, River City was taking in only about one-third of

projected revenues. After racking up \$8 million in operating losses in the first nine weeks, the partners were left with little choice but to "shut it down immediately," he says. The sudden closure in June left hundreds of creditors holding \$30 million in unpaid bills. Hemmeter now calls the project a "disastrous mistake," though he asserts that other gaming ventures made similar mistakes.

When it failed, Hemmeter's world

the \$15 million lent to him personally.

Resort Income's problems spawned at least three lawsuits by shareholders, who have watched their stock tumble from a high of 10 in early June to under 2 recently. In one, shareholders allege that Resort Income officers and directors breached their fiduciary duties and wasted the company's assets by allowing Resort Income to effectively serve as "Hemmeter's bank." In 1994, Resort Income paid Hemmeter-controlled RII

visors \$517,500 for services, which largely consisted of providing extensions of loans to various Hemmeter affiliates. Hemmeter denies the allegations. Resort Income declined to comment.

In July, Robinowitz, who parted company with Hemmeter in March, 1994, sued his former partner and

one of his companies for alleged failing to pay \$9 million in consulting fees. Robinowitz—who also has ownership stakes in Hemmeter Enterprises and Hemmeter's New Orleans casino ventures—now says getting involved with Hemmeter was "the biggest mistake and the worst decision of my life" because his investments are virtually worthless.

Hemmeter admits he owes Robinowitz money, but says the dispute is over a small amount.

Hemmeter vows eventually to repay Resort Income investors with proceeds from a \$100 million luxury resort he plans to develop on a Caribbean island of St. Maarten. That project, he says, will mark his return to resort hotel development. "I don't foresee us pursuing gaming opportunities any longer. We created the [luxury] resort. We think we know something about it," he says. Too bad it took a grueling four years in the casino business for Hemmeter to realize that.

By Stephanie Anderson Forest in Air, Calif.

## The Rise and Fall of Chris Hemmeter

**1976** Develops 1,260-room Hyatt Regency Waikiki, the first of five resorts he would build in Hawaii.

**1984** Nets \$188 million on sale of Hyatt Regency Waikiki and Hyatt Regency Maui.

**1988** Develops 1,244-room, \$360 million Hyatt Regency Waikoloa resort on the Big Island of Hawaii, featuring small boats to transport guests, who swim in a pool with dolphins. Hemmeter and investors later sell out, taking big profits.

**1990** Leaves Hawaii seeking to develop more than a dozen resort projects worldwide. But projects never materialize.

**1992** Opens two casinos in Colorado. Begins plans for a \$1 billion casino project in New Orleans.

**1993** Loses bid to build New Orleans casino, but snags one-third ownership stake. Wins license to operate gambling riverboat.

**1995** Opens elaborate River City casino complex, but runs out of money and

shuts it down in June—nine weeks after opening; Hemmeter unit thrust into bankruptcy in July by creditors. In August, Hemmeter removed as CEO of two of his companies after they rack up big losses.

DATA: BUSINESS WEEK



**OUT OF STEAM:** The idled Grand Palais riverboat

came tumbling down. "Hemmeter was so highly leveraged that all that was needed was to push that first domino over," says Randy Havre, a Honolulu-based investment analyst who has followed Hemmeter closely for years.

Other dominoes are also falling. Hemmeter Enterprises is on the verge of joining its Grand Palais Riverboat subsidiary in bankruptcy court. Hemmeter has been forced to turn over Hemmeter Enterprises, which had sales of \$45.5 million and losses of \$32.8 million in 1994, to bondholders, who will receive at least a 90% ownership stake.

**"HEMMETER'S BANK."** Resort Income Investors, which Hemmeter began in 1988 to raise cash for developments, is liquidating. That's because its entire \$36.6 million loan portfolio is tied to Hemmeter's New Orleans gaming ventures, Hemmeter personally, or other companies affiliated with him. He has said he wouldn't be able to repay the bulk of

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thinks Unisys  
is just a computer  
company.

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# THE BANKERS

In just-released court papers, Procter & Gamble lays out racketeering charges against Bankers Trust. The key evidence: Some 6,500 tape recordings

**I**t's Nov. 2, 1993, and two employees of Bankers Trust Co. are discussing a leveraged derivative deal the bank had recently sold to Procter & Gamble Co. "They would never know. They would never be able to know how much money was taken out of that," says one employee, referring to the huge profits the bank stood to make on the transaction. "Never, no way, no way," replies her colleague. "That's the beauty of Bankers Trust."

That dialogue was automatically picked up by a Bankers Trust recording system—similar to those at other financial institutions—that routinely tapes conversations involving transactions, mainly to settle disputes over trades. It's part of a mountain of evidence—6,500 tapes, as well as 300,000 pages of written material—that forms the basis of a major legal assault by P&G against the bank. P&G contends that the 1993 conversation is just one of many showing that Bankers Trust deliberately misled and deceived and kept the company in the dark about key aspects of the derivatives the bank was selling.

*BUSINESS WEEK was barred by court order from publishing early versions of this story. An account of the legal battle to remove the restraint begins on page 114.*

## The Tale Of The Tapes

*Procter & Gamble, through discovery, obtained 6,500 tape recordings, as well as 300,000 pages of documents from Bankers Trust. The material concerned nine Bankers Trust clients who lost money dealing with the bank. From this evidence, P&G is alleging that Bankers Trust:*

- Engaged in a pervasive pattern of fraud spanning a number of years and involving numerous victims
- Induced customers to purchase complex derivative deals that produced high profits for the bank and often big losses for many of its clients
- Misrepresented to clients the pricing, current value and

- risks of the products it sold
- Refused to share its secret pricing models and other proprietary devices
- Caused customers who had suffered losses to engage in ever more complex transactions that were supposed to recover losses but that often brought on even more problems

DATA, BUSINESS WEEK, COURT FILINGS



# TRUST

One of the most powerful, profitable, and aggressive in the world, Bankers Trust has been humbled over the last 18 months by a series of debacles in its core derivatives business, with numerous clients of the bank sustaining large losses. P&G took a \$102 million after-tax charge for its losses on Bankers' derivatives, perhaps the largest of any of its customers. Several other clients have also sued the bank. And the Securities & Exchange Commission, the Commodity Futures Trading Commission, and the Federal Reserve Bank of New York have all investigated Bankers' derivatives sales practices and sanctioned or censured the bank.

Procter & Gamble's fight with Bankers Trust is taking a new and far more ominous turn for the bank. On Sept. 1, P&G filed a motion with the United States District Court in the Western Division of the Southern District of Ohio to add RICO (racketeering-influenced and corrupt organization) to its list of allegations against the New York bank and its affiliate, BT Securities Corporation. Supporting documents, which contain numerous excerpts of conversations by the bank's employees, were sealed until Oct. 3. The same day, district court judge John S. Jones approved the P&G RICO motion.

Some portions of the tapes, mainly concerning Gibson Greetings, a Bankers Trust client, became public last year. But the released portions, some of which are potentially incriminating, are much more extensive. They focus on eight P&G customers besides P&G. The allegations of three of them—Sandoz, Inc., and Jefferson Smurfit—had not previously been detailed. Other alleged victims in the pending complaint are Gibson Greetings, Equity Group Inc., Adimira Rayapratama, Air Products & Chemicals, and Federal Paper Board (table, page 111).

**EMAIL** P&G uses evidence of alleged wrongdoing against its clients to buttress the racketeering charges, which read as a showing of broad, systemic fraud. Asserts the P&G filing, "It is now apparent that Defendants' treatment of P&G is not an isolated incident or a 'garden-variety fraud,' but is part of a pattern of mail, wire, and securities fraud spanning a number of years and involving multiple victims." In a 400-page filing opposing P&G's claims, Bankers says P&G plainly has proposed adding civil RICO claims at this stage for their *in terrorem* effect; laymen would call it blackmail. The bank says further that "The real impetus for the charges is P&G's hope that legitimate criticism of decisions by P&G's senior management and Treasury Dept. staff will be lost at trial in a sea of accusations about customers

# TAPES

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF OHIO  
WESTERN DIVISION

THE PROCTER & GAMBLE COMPANY,  
Plaintiff,  
vs.  
BANKERS TRUST COMPANY  
and  
BT SECURITIES CORPORATION,  
Defendants.

Case No. C-1-94-735  
(Judge Finkens)

SEP 1 1994

MEMORANDUM IN SUPPORT OF  
THE PROCTER & GAMBLE  
COMPANY'S MOTION FOR  
LEAVE TO AMEND COMPLAINT  
(FILED UNDER SEAL PURSUANT  
TO PROTECTIVE ORDER)

**INTRODUCTION**

After months spent piecing together the complex details of the Defendants' business practices, it has become apparent that Bankers Trust Company ("Bankers Trust") and BT Securities Corporation have engaged in a pattern of fraud and misrepresentation going well beyond their victimization of The Procter & Gamble Company ("P&G"). P&G was but one of a series of companies lied to, exploited and cheated by the Defendants. The evidence leads to one inescapable conclusion — that the Defendants were engaged in a pattern of activity falling squarely within the provisions of the RICO statute.

PROCTER & GAMBLE

Two Procter & Gamble Plaza



other than P&G, and that Bankers Trust can be vilified by the sheer number of P&G's accusations." In a statement released after P&G's documents were unsealed, Bankers said that "What P&G has done is to use material we provided to man-

ufacture a distorted view of transactions, markets, individuals, and the corporation in

a manner designed to serve its own objectives and to obscure P&G's own accountability." BW attempted to solicit comments from Bankers Trust's directors, but they either refused, referred calls to the bank, or could not be reached.

P&G provides a detailed case for its side. To substantiate its claim that a "culture of greed and duplicity" was an element of the general climate in parts of Bankers' derivatives business, P&G cites a videotaped training session for new employees. At the session, a bank employee tells his charges that, in a hypothetical derivative transaction among Sony, IBM, and Bankers Trust, "what Bankers Trust can do for Sony and IBM is get in the middle and rip them off—take a little money." The employee then adds: "Let me take that back. I just realized that I'm being filmed." A Bankers spokesman played six minutes of the videotape of the session for BW, which the bank says lends support to the bank's contention that the employee's comment was "a very poor attempt at humor, but nothing more," in an "otherwise dull presentation" and that the comment was taken out of context.

According to P&G: "Fraud was so pervasive and institutionalized that Bankers Trust employees used the acronym 'ROF'—short for rip-off factor, to describe one method of fleecing clients." An internal document about a proposed

derivative for Federal Paper Board allegedly says that Bankers would make \$1.6 million on the deal, including a "7 [basis point] rip-off factor." In a different instance, two Bankers employees are discussing a client's loss on a trade. One tells the other: "Pad the number a little bit." P&G quotes another Bankers Trust employee saying to a colleague: "For business, you know? Lure people into that calm and then totally f— 'em."

In responding to conversations by Bankers Trust employees quoted in this story, a bank spokesman says that "the stupid and crude comments between Bankers employees on these tapes were the basis for our disciplinary actions against these individuals last year." A number of employees quoted in the documents have left Bankers, been disciplined, or been reassigned.

**UPPING THE ANTE.** John E. Pepper, P&G's new CEO, will comment on the Bankers situation. But the racketeer charge shows he is maintaining the company's well-known aggressive legal posture. A P&G spokeswoman says: "We reviewed hundreds of recorded telephone conversations and thousands of documents through discovery and believe that P&G's RICO claim was appropriate. We plan to proceed with the case." The company further claims that it expects to uncover additional evidence.

In its filings, P&G details three primary schemes Bankers allegedly used to defraud its clients. It says the bank fraudulently induced clients to buy complex derivatives, misrepresented the contracts' value, and then induced clients to buy additional complex derivatives, either for further alleged gains or to stanch losses. It quotes one banker describing a client's portfolio as being in total disarray: "It

## THE FLOODWATERS ARE RISING AROUND BANKERS TRUST

Charles S. Sanford Jr. seemed upbeat and jocular as he spoke to the standing-room-only crowd on a sunny September Friday. The chairman of Bankers Trust was addressing a conference on "Women on Wall Street" sponsored by a women's network at Bankers Trust. After he told the members of his audience that he was supportive of their efforts, he warned them that he might "come back for the politics and power section." Amid the laughter, Sanford added: "I need some coaching."

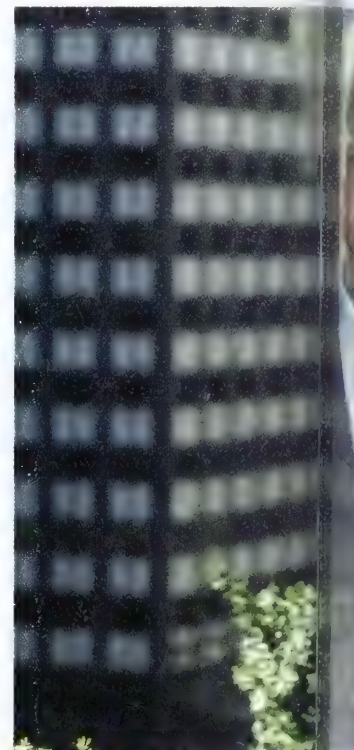
Unfortunately, Sanford and Bankers may need a lot more than that. The bank is still reeling from the after-shocks of the huge derivatives losses suffered by many of its clients, a number of whom have stopped doing business with the bank. One derivative expert says he is aware of half-a-dozen companies that have lost money on Bankers' derivatives but that have not been identified. In a biennial poll of derivatives users by *Treasury & Risk Management* magazine, which ranked banks on the quality of service they provide in the derivatives market,

Bankers dropped from first in 1993 to fifth in 1995.

Bankers' derivatives business, which generated 42% of 1994 earnings, lost \$171 million in the first half of the year. Sources close to Bankers say the bank's other businesses, such as private banking and asset management, are also suffering as clients have become increasingly wary of doing business with a bank with Bankers' problems.

**PROGRESS?** A Bankers spokesman responds that "after our first-quarter losses we feel we've made strong, steady progress toward a return to a competitive financial performance." But most analysts expect overall earnings to be only mediocre for a major bank, 15% return on equity or less. Says Raphael Soifer of Brown Brothers Harriman: "This raises the long-term question about where Bankers Trust goes." That level of performance is below the returns being generated by other money-center banks, even those concentrated in businesses less volatile than Bankers'.

Whether or not Bankers can contin-



ue as an independent company to be seen. Investment banks shopped the bank around, all but out Bankers' bidding. One source to the bank says the bank's an emergency meeting in mid-



# P&G has...manufacture[d] a distorted view of transactions, markets, individuals, and the corporation...to serve its own objectives and obscure P&G's own accountability"

## BANKERS TRUST PRESS RELEASE

comes out in the press, it is the most insane mess of anything I've ever, ever seen...they just kept trying to get them out of losses...Everything they put in [the account] lost."

The new charges, which claim \$195.5 million in damages, prove extremely embarrassing to the bank—or worse. The company found guilty of civil RICO charges must pay treble damages and plaintiffs' legal costs. Such an outcome would push Bankers to settle the suit regardless of its culpability. "It ups the ante," says attorney Robert Plotkin of Hastings, Janofsky & Walker in Washington. In addition, the case could become unsettled by the appearance of a corrupt officer, and senior management could come under even more pressure.

Each side of the dispute between Bankers Trust and its clients suffered losses may depend on whether the clients were naive and should have known what they were getting or whether Bankers Trust deliberately deceived them. Bankers Trust strongly argues the latter.

from those assets. Besides lowering financing costs, buyers may use derivatives to manage risk or speculate on interest and currency rates.

P&G seemed to be an active and sophisticated player in the financial markets: It had \$5 billion in long-term debt outstanding, and it carefully managed its financing costs. In court filings, Bankers describes P&G as "sophisticated, experienced, and knowledgeable about the use of interest-rate derivative contracts and the risks presented by those contracts." The bank adds: "Although P&G would like this court to believe that it is a naive and unsophisticated user of derivatives transactions, the fact is that as part of its regular course of business and with authorization from top management...P&G's Treasury Department managed a large and sophisticated portfolio of derivative transactions." P&G, the bank says, was a party to derivatives tied to assets with a value of more than \$6 billion as of June, 1993.

In its memorandum opposing P&G's motion, Bankers presents documents, including handwritten notes apparently by



**CHAIRMAN SANFORD:** *He plans to retire by next summer*

mission charges regarding its derivatives sales practices. Derrick Cephas, a former New York State Banking Commissioner and a partner at the law firm of Cadwalader, Wickersham & Taft, and Benjamin R. Civiletti, a former U.S. Attorney General and a partner at Baltimore's Venable, Baetjer, Howard & Civiletti, are auditing the financial institution's operations. Their report will likely be released before the

to see much of the uncertainty resolved, having somewhat abruptly announced plans to retire next summer at the age of 60. Many sources close to the bank felt that President Eugene B. Shanks Jr. would get the top job, despite the fact that he was instrumental in building up the bank's derivatives business.

**RUMORS.** On Sept. 21, though, the bank hired Frank N. Newman, former Deputy Treasury Secretary, to be a senior vice-chairman and director. That has led many Bankers observers to wager that the succession question has been resolved. One rumor has Newman taking the reins and the bank establishing a co-presidency of the bank shared by Yves de Balman, co-head of global investment banking, and Kelly Doherty, head of proprietary trading. Bankers Trust says that its board "has stated that it is in the process of identifying a successor to Sanford. That process continues."

Bankers Trust is a long way from the days when it dominated the market for complex derivatives. Sanford might wish that seminars on power and politics would be all that it takes to turn the bank around. What Bankers Trust really needs, though, is to live up to its name.

*By Kelley Holland, with Phillip L. Zweig, in New York*

to discuss an acquisition, the bank has declined comment. The bank is still under regulatory scrutiny as part of Bankers' settlement with the Securities & Exchange Commission and the Commodity Futures Trading Com-

mission end of the year.

All the turmoil represents a stunning comedown for Sanford, long regarded as one of the brightest and most visionary bankers in the country. Sanford, however, will not be around



Edwin Artzt, P&G's chief executive officer at the time, that suggest the Cincinnati company was knowingly stepping up the riskiness of its financing activities when it entered into the disputed transactions with Bankers. P&G says the note does not apply to debt management or to the transactions in the litigation.

## Cover Story

On Nov. 2, 1993, P&G agreed to an offer from Bankers Trust to buy a leveraged derivative product. Leveraged derivatives are a particularly complex type of derivative, and their value can fluctuate to an even greater degree than ordinary, plain-vanilla derivatives. The contract called for P&G to make variable-rate payments to Bankers, with the rate to be set over the next several months.

It is not clear whether P&G knew what the cost of getting out of the contract might be, and P&G has since acknowledged that its internal procedures were not followed when it agreed to this derivative. The company also ultimately reassigned two employees involved with the derivatives, and its treasurer, Raymond D. Mains, who later elected to retire early. Mains declined to comment. But at the time, the company believed it might get interest costs below what they would have been otherwise.

The derivative seemed to work fine at first. Indeed, P&G was sufficiently satisfied to agree to a second leveraged derivative contract on Feb. 14, 1994. But P&G began encountering serious problems almost immediately. On Feb. 4, interest rates had begun rising after more than three years of near-continuous decline. The higher rates sharply pushed up P&G's payments to Bankers under the terms of the complex derivatives.

**"IRRESPONSIBLE AND REGRETTABLE."** On Feb. 22, P&G claims, Bankers told the company that at that day's rate, P&G stood to pay Bankers an increased interest rate of 4.5 percentage points above the commercial-paper rate on its Nov. 2 derivative, bringing its extra financing costs to over \$40 million. P&G says its officials were alarmed by the unexpectedly large amount. They charge that when they asked Bankers for an explanation, they learned that the bank was using a proprietary model to figure the costs. Bankers, P&G's complaint says, "stated that P&G was bound by a pricing model which [Bankers] did not disclose to the very party that it asserted was bound by such model."

**“What Bankers Trust can do for Sony and IBM is get in the middle and rip them off—take a little money.... Let me take that back, I just realized I’m being filmed”**

— P&G COURT FILING THAT ALLEGEDLY REFLECTS WHAT WAS SAID AT A BANKERS TRUST VIDEOTAPED TRAINING SESSION

Bankers Trust's court filings include a transcript of an October, 1993, conversation between Bankers and P&G in which Bankers apparently shows a P&G treasury employee how to calculate its rate on the Nov. 2 derivative. Bankers says this transcript demonstrates that P&G clearly knew how its derivative would perform. The bank also cites file memos from three P&G employees that it says indicate that P&G was made aware of the rising rates on its Nov. 2 derivative in early or mid-February, 1994. As for the Feb. 14 derivative, Bankers presents as evidence notes by P&G's chief financial officer, Erik Nelson, that it says show that he did not feel P&G was misled on that derivative's terms.



**P&G'S PEPPER:** *The aggressive legal stance continues*

P&G, however, claims that those notes were written before the company learned all it now knows about that derivative. And it says Bankers employees were clearly and almost obviously trying to deceive it from the day the derivative contract was initiated. P&G cites a taped conversation between Bankers employees about the Nov. 2 P&G contract where one says, "Do they [P&G] understand that? What they did?" The other replies: "No. They understand what they did but they don't understand the leverage, no." The first employee then responds: "But I mean...how much do they want to tell them. What is your obligation to them?" The second employee answers: "I'll tell them if it goes wrong, what does that mean in a payout formula..."

Bankers employees were often given a share of the big profits they were booking from the trading according to P&G. The second employee quoted above says P&G undertook a derivatives trading option trade as part of a derivatives contract, and Bankers paid P&G only what that option was worth. The employee allegedly remarks: "This could be a massive huge future gravy train." He allegedly discussed how significant one of P&G's contracts had been for Bankers, saying, "This is a wet dream."

In April, P&G claims, Bankers Trust gave the company charts showing that it would have had to pay a penalty to get out of its Nov. 2 contract almost from Day One. According to P&G's documents, one Bankers salesman, discussing an agreement to enter into the Nov. 2 contract, said "we set up." P&G claims that, unbeknownst to the company at the time, there were periods when Bankers' model calculations showed that P&G's potential penalty payment to exit the derivative was rising even when interest rates were falling.

P&G claims that around that time, some Bankers employees



themselves worrying about the suitability of their activities. It cites a March, 1994, conversation between two employees where one said he had "fears of SEC probes." "This was always...made up of polluted water," one says. The other recalls telling a colleague that "as soon as we start selling dynamite, maybe we'll have a good business." Ultimately locked in interest rates on both of the leveraged derivatives in dispute. But it alleges that by the time they had done so, in April, 1994, its financing costs stood to be \$195.5 million higher than they should have been. Same month, P&G said: "We are seriously considering our options relative to Bankers Trust."

In a statement, Bankers concedes that some of the taped conversations "were irresponsible and regrettable." But it says the remarks fall short of proving the deception P&G alleges. Instead, it produces evidence in court filings that

top executives and their own people for the investment blunders. "Rather than putting its house in order, accepting its losses, P&G chose instead of this lawsuit." It is also making its fraud claims against Bankers' dealing with their clients. Sev-

eral alleged victims have already gone public with their grievances. Gibson Greetings has settled a lawsuit with Bankers, as has Equity Group Holdings. Adimitra Rayana also sued, claiming RICO violations, although a ruling on its suit on jurisdictional grounds is under appeal. Federal Paper Board has settled with Bankers. Bankers says in court filings that it needs much more information to refute P&G's allegations about other companies.

P&G filing provides new information about three Bankers clients whose relationship with the bank has not been previously detailed. In the case of Sandoz Corp., P&G says that Sandoz entered into a leveraged derivative contract with Bankers on Jan. 31, 1994. Beginning in February, P&G says, employees of BT Securities knowingly misled Sandoz about the value of its contract by \$5 million. Sandoz allegedly ended its derivative contract nine months later on Bankers' recommendation, losing some \$25 million in the process. At one point, P&G asserts that Sandoz paid \$4.2 million to modify its derivative contract when the change increased its cost by only \$2.9 million. That netted Sandoz over \$1.4 million.

**ELEMENT?** P&G also claims that a Bankers Trust representative, knowing that the move would generate a large profit for Bankers, told Sandoz that the "convenient" way to manage its position was to double its exposure while ignoring the interest rate above which it would be hit with higher payments under the contract. But on Feb. 22, discovering that Bankers did not have the proper authority to cover such a change, the Bankers reversed course—and began encouraging Sandoz to reduce its position. P&G alleges that Sandoz lost \$78.5 million in dealing with Bankers. Sandoz General Counsel Robert L. Thompson says: "We settled a matter with Bankers Trust.

The terms of the settlement are confidential," and he adds that Sandoz continues to have a "productive" relationship with Bankers.

As for Sequa Corp., P&G alleges that Bankers sold it a leveraged derivative—similar to P&G's Nov. 2 contract—on Oct. 1, 1993.

In December, Bankers

allegedly proposed various amendments to the contract that it told Sequa were costless. But, says P&G, an internal Bankers Trust phone call described it as having a negative value for Sequa of \$600,000 and a profit for Bankers Trust of \$200,000.

With interest rates rising, P&G says Sequa terminated half of the contract in February, 1994, at a cost of \$2.5 million. Sequa allegedly terminated the rest a month later at a cost of \$4.5 million, financing that with another transaction in which it

was to pay Bankers \$6 million over the ensuing two years. Total alleged loss: \$7.5 million. Sequa declined comment.

In the case of Jefferson Smurfit Corp., P&G alleges that Smurfit entered into a leveraged derivative contract in May, 1993. The derivative quickly be-

gan losing value, P&G says, and Smurfit closed out the contract and was paid \$1.17 million by Bankers. But that was at a time, P&G claims, when Bankers internally valued Smurfit's position in the contract at \$4.4 million.

Smurfit agreed to another leveraged-derivative contract in December, 1993, according to P&G. The company says Bankers "induced Smurfit to amend this swap [a kind of derivative] 11 times before it was finally unwound in September, 1994." Meanwhile, the value of Smurfit's contract was declining. P&G says Bankers did not tell Smurfit, however. Alleges P&G: "As early as February, 1994, BT Securities marketers discussed the fact that Smurfit was \$5 [million] or \$6 million down on the deal and that Smurfit's Treasurer 'has no clue' about how far 'underwater' his company was on the transaction."

At one point, P&G claims, Bankers Trust employees discussed showing Jefferson Smurfit some information regarding one of its derivatives, and one employee said: "...what we show them is gonna be kind of baloney...." Ultimately, P&G says, Smurfit lost more than \$2.4 million on its derivatives dealings with Bankers. Smurfit says it is not aware of suffering any losses on derivatives with Bankers.

What's next for Bankers Trust? It's possible that the bank will settle with P&G rather than endure the possible playing of hours of incriminating tapes in open court. The Securities & Exchange Commission, which investigated Bankers Trust's derivatives sales practices, forced a deeply embarrassing settlement on the firm. The SEC says it is continuing to investigate evidence of individual wrongdoing. One thing, though, is clear: The "massive huge future gravy train" has been permanently derailed.

By Kelley Holland and Linda Himelstein in New York, with Zachary Schiller in Cleveland

## Cover Story

# "Fraud was so pervasive...that Bankers Trust employees used the acronym ROF—short for rip-off factor, to describe one method of fleecing clients"

— P&G COURT FILING

## Victims?

*Companies that Procter & Gamble says lost money on derivatives due to Bankers Trust's allegedly fraudulent sales practices*

| COMPANY                   | LOSS<br>MILLIONS |
|---------------------------|------------------|
| PROCTER & GAMBLE          | \$195.5          |
| AIR PRODUCTS              | 105.8            |
| SANDOZ                    | 78.5             |
| P.T. ADIMITRA RAYAPRATAMA | 50.0             |
| FEDERAL PAPER BOARD       | 47.0             |
| GIBSON GREETINGS          | 23.0             |
| EQUITY GROUP HOLDINGS     | 11.2             |
| SEQUA                     | 7.5              |
| JEFFERSON SMURFIT         | over 2.4         |

DATA: PROCTER & GAMBLE CO., COURT FILINGS





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inventory risk



# BUSINESS WEEK VS. THE JUDGE

The magazine gets to publish its story—but First Amendment issues remain unresolved

**B**loody gloves and shoe prints it wasn't. But as First Amendment cases go, this proved pretty taut courtroom drama:

"Mr. Holley, what is your home telephone number?"

"254-8159."

"Mr. Holley, did you receive a call at your home on the afternoon of Sept. 13 from someone at BUSINESS WEEK?"

In a Cincinnati federal court on Sept. 27, some thought they saw Steven L. Holley blanch under the cross-examination. It surely was an unlikely moment: A star antitrust litigator, Holley had made partner in 1991, at age 33, at Sullivan & Cromwell, a top-drawer Wall Street law firm. Now, he was in trouble. Having already admitted to providing BUSINESS WEEK with a copy of sealed court documents from a case involving his firm's client, Bankers Trust Co., Holley was about to be confronted with phone records



**FREEDOM OF THE PRESSES:** *The current issue rolls*

contradicting his assertion that he didn't learn the papers were confidential until more than a year later.

Holley's seemingly damning testimony in New York's legal case was buzzing. Yet ultimately, barely affected the outcome of a three-week constitutional battle pitting BUSINESS WEEK against Bankers Trust, Procter & Gamble Co., and District Court Judge John Feikens, who on Sept. 3 had enjoined the magazine from printing a story

based on the documents Holley provided.

On Oct. 3, Feikens granted a motion by P&G to add racketeering charges to its derivatives-related claim against Bankers Trust, unsealing the much-discussed documents and parties, including BUSINESS WEEK. At the same time, though ruling that the magazine had acted "unlawfully," the judge made permanent his injunction against the magazine's use

## (Sealed) Paper Trail

*How BUSINESS WEEK became tangled in litigation between Procter & Gamble and Bankers Trust*

### AUGUST 31

BUSINESS WEEK Cleveland Bureau Chief Zachary Schiller learns that P&G will amend its case against Bankers Trust with a new filing. (In testimony, Schiller said this information comes from P&G spokesman Gregory Rossiter; Rossiter denied this.)

### SEPTEMBER 1

P&G moves to add racketeering charges to its complaint. On Sept. 6, at Schiller's behest, freelance journalist Joseph Levy unearths P&G's motion in U.S. District Court in Cincinnati.

### SEPTEMBER 7

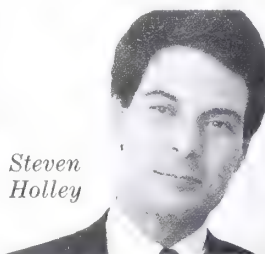
Schiller confirms that at least portions of P&G's amended claim are under court seal.

### SEPTEMBER 12

Legal Affairs Editor Linda Himelstein obtains the documents from Steven Holley, a partner at Sullivan & Cromwell, Bankers Trust's outside counsel. At the time, neither Himelstein nor Holley know the documents are sealed.

### SEPTEMBER 13

Bankers Trust and P&G learn BUSINESS WEEK has obtained



Steven  
Holley

the sealed papers and ask District Court Judge John Feikens to enjoin publication of the resulting story. Feikens issues the order at 6 p.m. without giving the magazine prior warning; BUSINESS WEEK holds the story.

### SEPTEMBER 19

The appeals court for the Sixth Circuit refuses a BUSINESS WEEK request to lift the restraining order.

### SEPTEMBER 21

Supreme Court Justice John Paul Stevens refuses to stay the order, returning the case to district court. Before Feikens, Himelstein declines to identify Holley as her source. Later, confronted by partners, Holley admits to his actions.

### SEPTEMBER 27

Holley tells the court he breached the protective order but denies knowing before Sept. 21 that the papers had been sealed.

### OCTOBER 3

Feikens allows the amended claim, making the documents public. But he makes permanent the injunction against BUSINESS WEEK. The magazine appeals.



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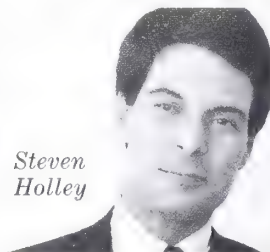
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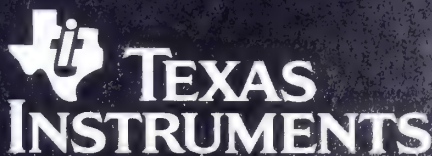
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the original set of documents. "I cannot permit BUSINESS WEEK to snub its nose at court orders," he wrote. "The integrity of a court and the entire judicial system requires that its orders be acknowledged and obeyed."

## Cover Story

ently thinks he's splitting the baby," said Kenneth M. Vittor, general counsel of BUSINESS WEEK's parent, The McGraw-Hill Companies. BUSINESS WEEK, after all, was allowed to print its story; the injunction did not prevent the magazine from obtaining a new copy of the now-public papers. "This is a victory in that we are now able to publish the story," says Stephen B. Shepard, editor-in-chief.

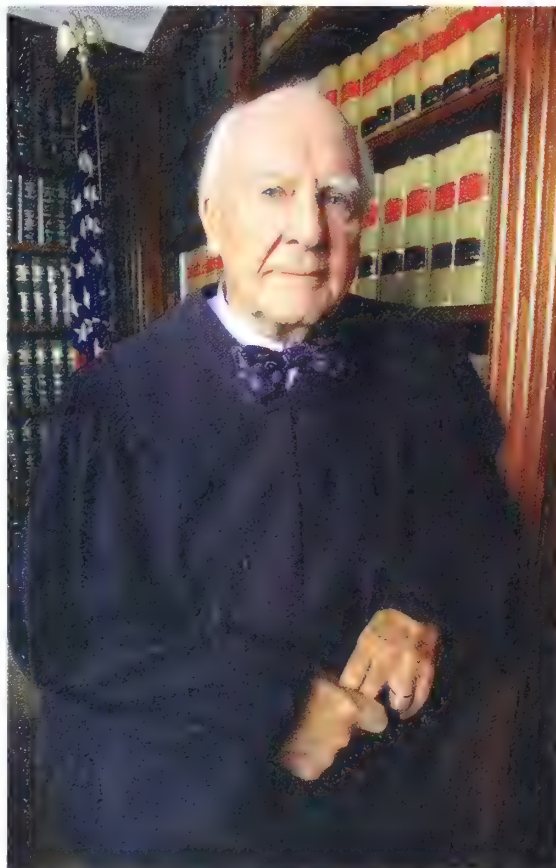
Yet Feikens left unresolved the essential First Amendment question: Does freedom of the press supercede other concerns, notably preserving the sanctity of the court? The Supreme Court has ruled consistently that it does, specifically in a 1978 decision allowing Landmark Communications Inc. to publish information about a confidential investigation of a Judicial Review Commission in Virginia. Feikens' injunction is "absolutely at odds with 100 years of American law," says attorney Floyd Abrams, because it collides head-on with the prior-restraint doctrine, barring the government from blocking publication in almost all circumstances.

Ironically, the testimony in Feikens' courtroom, along with reams of supporting notes, internal electronic-mail messages, and other documents, dealt little with the First Amendment question. Rather, the judge simply wanted to establish how the sealed documents had escaped his court in the first place. A clear answer emerged. Yet conflicting testimony—often setting the magazine's journalists against their own sources—left some unsettling loose ends.

**CONTRADICTIONS.** The tale: On Aug. 31, according to his own notes, BUSINESS WEEK Cleveland Bureau Manager Zachary Schiller took a call from Gregory Rossiter, a supervisor of corporate communications at P&G. Rossiter told Schiller that P&G would be making a filing in its Bankers Trust case, likely the next day. "He was telling me, 'You should get this because if you're doing some sort of story, you're going to want to include this,'" Schiller recalls. In his testimony, Rossiter denied that this conversation took place, even when presented with Schiller's copious notes of the exchange.

In fact, P&G did file the motion on Sept. 1 to amend its claim. Some 300 pages of supporting documents were sealed under an earlier protective order. That order, however, was unnoted anywhere in the public, three-page motion obtained

Feikens' decision sent a mixed, controversial message. "This is a judge who appar-



**"I cannot permit BUSINESS WEEK to snub its nose at court orders.... The integrity of a court... requires that its orders be obeyed."**

—JOHN FEIKENS, U.S. District Court Judge

on Sept. 6 from the U.S. District Court clerk's office by Joseph Levy, a freelance journalist working for BUSINESS WEEK. Schiller says he did not learn the papers had been sealed until the next day; Rossiter testified he told Schiller on Sept. 6 that the papers were confidential—again contradicting Schiller's notes.

On Sept. 6, Schiller told the magazine's legal affairs editor Linda Himelstein, about the Racketeer-Influenced & Corrupt Organizations Act (RICO) filing—and indicated, being known about the protective order, that he had been unable to locate the supporting documents. Himelstein agreed to try to find the papers independently. The two say they did not talk again until Sept. 13.

In the meantime, Himelstein placed a call to Holley. The two had talked regularly for two years. Holley had aggressively courted the media on behalf of the band Pearl Jam, which filed an antitrust complaint against Ticketmaster Corp., the giant ticket agency Himelstein profiled in *June*. He also had represented Microsoft Corp. in its antitrust battle. **NO WARNING.** Holley returned Himelstein's call on Sept. 12 and agreed to locate a copy for her P&G's RICO motion. According to his testimony, Holley got the papers from Richard C. Pepperman II, an associate assigned to the Bankers Trust case. Pepperman, Holley testified, did not ask if Holley wanted the papers, nor did he mention the protective order. Pepperman declined to be interviewed, referring BUSINESS WEEK to Ricardo A. Mestres Jr., Sullam & Cromwell's chairman. Mestres did not return calls.

Himelstein received the documents via messenger at 5 p.m. that day. After skimming the contents, she and Kelley Holley, BUSINESS WEEK's money and banking editor, began a story on P&G's RICO charges. Only the next morning, both reporters say, did she find on the filing's fourth page the statement: "Filed under seal pursuant to protective order."

That afternoon, Himelstein called Holley's residence to ask him to her discovery. McGraw-Hill phone records indicate that she called from her phone to his lasted only two minutes. Himelstein testified that when Holley learned of the protective order, he exclaimed "Oh, shit!," then asked that the story not be run. When Himelstein said it would be published, she testified, Holley asked that his role be kept secret. She agreed.

In court on Sept. 27, Holley denied this conversation took place, even after being confronted with the McGraw-Hill computerized phone records. He testified that on Sept. 13 he left New York to visit his parents in Muskegon, Mich., where he read only *The Muskegon Chronicle*; he heard nothing about the BUSINESS WEEK injunction, he told the court, until



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Sept. 21. In fact, the *Chronicle* published a brief account of the BUSINESS WEEK case on Sept. 15.

If Holley knew that the protective order had been breached but failed to inform the court, both he and Sullivan & Cromwell, as parties to the dispute via their client, Bankers Trust, would have violated the

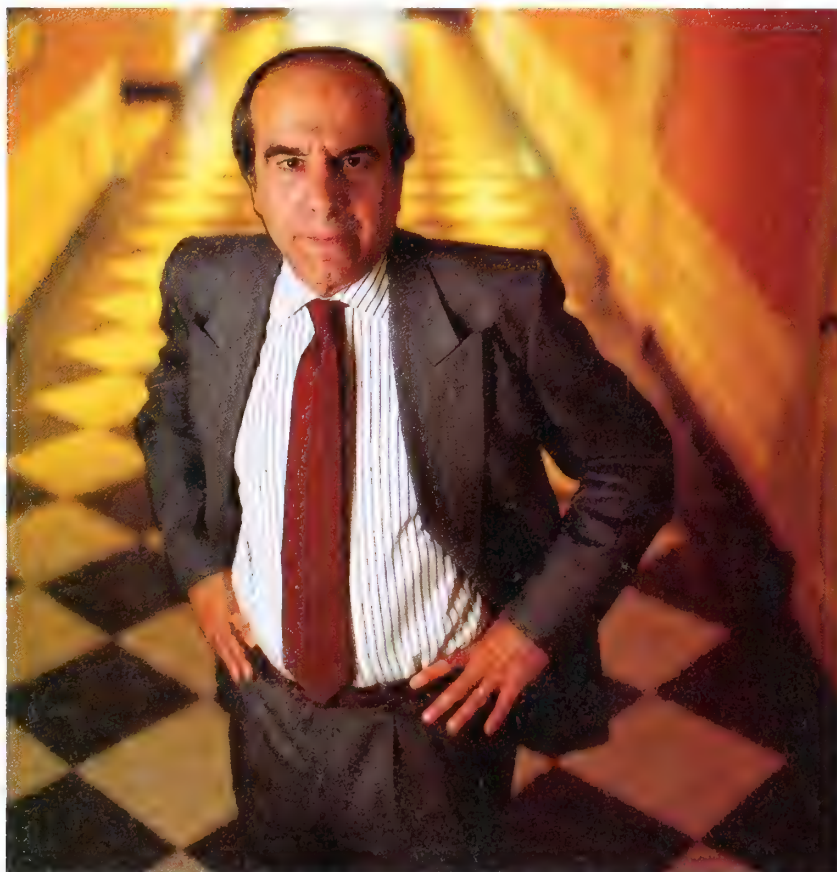
## Cover Story

terms of the order, although neither has been charged.

Bankers Trust and Procter & Gamble learned of the prospective story on Sept. 13 and asked Feikens for an injunction that would bar BUSINESS WEEK from publishing the piece. The order arrived without prior warning—violating federal rules

who, noting that the magazine had “doggedly avoided such a proceeding,” seemed annoyed that he had been bypassed. At the Sept. 21 hearing, Himmelstein was called on to identify her source; on 10 occasions during cross-examination she invoked the First Amendment and state shield laws to protect her confidential relationship with Holley. The judge did, however, compel her to place the source in New York State.

That concession allowed Himmelstein to claim confidentiality under New York State shield laws, which, unlike Ohio statutes, protect magazine, as well as newspaper, journalists. On that day, apparently guided by a record in the firm’s messenger log, a Sullivan & Cromwell partner asked Holley whether



“This is a victory in that we are now able to publish the story.”

— STEPHEN SHEPARD,  
BUSINESS WEEK Editor-In-Chief

was the source of the document. Holley admitted he was.

Holley remains at Sullivan & Cromwell. But his breach has produced unexpected ripple effects. In cross-examination by McGraw-Hill’s outside counsel to establish the confidential nature of his relationship with Himmelstein, which he denied, Holley learned that, in the midst of Microsoft’s battle with the Justice Dept. antitrust chief Anne K. Bingaman, he said that, “Everyone on [Bingaman’s] professional staff thinks that she’s out of her mind.” Holley apologized to Bingaman in a letter Oct. 2, calling his remarks “inappropriate.” Bingaman wrote back the next day: “Apology accepted!”

Ultimately, Feikens didn’t buy BUSINESS WEEK’s testimony. Accusing the magazine of “duplicity,” he ruled that Schiller’s knowledge of the protective order could be imputed to BUSINESS WEEK as an organization.

Thus, he said, Himmelstein’s acquisition of documents that the magazine knew to be confidential constituted an illegal act—justifying, Feikens said, his prior restraint of publication.

From a First Amendment perspective, it was a troubling conclusion, as was Justice Stevens’ contention that “the manner in which BUSINESS WEEK came into possession of the information it seeks to publish may have a bearing on its right to do so.” If the magazine’s Oct. 3 appeal is heard, “I’m very dubious that the legality of the method of acquiring the information will end up being a factor in the development of prior restraint doctrine,” says Lee C. Bollinger, a constitutional scholar and provost at Dartmouth College. More to the point, says BUSINESS WEEK’s Shepard, “We’re free to ask for things and they’re free to say no.”

How the dispute is resolved may well prove precedent-setting. If the courts refuse to hear an appeal, or if they decide that maintaining confidentiality of discovery materials justifies prior restraint, they would retreat dramatically from precedent. It’s an unlikely outcome—but for many journalists, even the possibility is unsettling.

By Keith H. Hammonds in New York, with Cathleen Yang in Washington

governing civil procedure—on Vittor’s fax machine at 6 p.m. After failing to contact Feikens, McGraw-Hill’s local counsel in Cincinnati reached Danny J. Boggs, a judge of the Sixth Circuit Court of Appeals. But Boggs declined to act on the injunction. Shepard and Vittor decided to hold the story. “We followed the same strategy as *The New York Times* did in the Pentagon Papers case—obey the injunction, then fight it immediately in court,” Shepard says.

**STRONGER SHIELD.** McGraw-Hill pursued a formal appeal to the Sixth Circuit, which on Sept. 19 decided on procedural grounds not to act, and then to Justice John Paul Stevens of the Supreme Court. In legal circles, that strategy was controversial. Vittor argues that, faced with an apparently permanent order that could not be legally or factually sustained, McGraw-Hill was obliged to appeal immediately. Even so, the company should have given Feikens “a chance to correct his mistake,” says Burt Neuborne, a professor of law at New York University and former legal director of the American Civil Liberties Union. Indeed, in refusing to stay the injunction on Sept. 21, Stevens reprimanded McGraw-Hill for not seeking remedy with Feikens first.

BUSINESS WEEK landed back in the courtroom of Feikens,



# American Competitiveness

**GAINING AN EDGE THROUGH  
STRATEGIC STANDARDIZATION**



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# Competing through Standardization

global competition intensifies, leading American businesses are increasingly adopting an emerging management discipline as part of their business strategy.

This discipline is called strategic standardization, and the effective management of it can open new markets, increase sales, reduce trade barriers, and ensure a company's competitive edge and profitability. European companies have used this same discipline to their own advantage for some time – to ensure a strong leadership position in the global market – U.S. business leaders need to do the same. Contrary to the view of standardization as only a technical issue, it is in fact a critical business strategy with implications

for market structure, anti-trust, product liability, policy and regulation, new product development, occupational health and safety, the environment, government acquisition reform, and our very quality of life. In a period of otherwise shrinking corporate budgets, companies as diverse as



Ameritech, Ford, and Polaroid have set up offices of strategic standardization.

Americans' daily lives depend on standards that we take for granted, which – like air – are everywhere, from the products we use, the food we

eat, how we communicate, work, play, travel, and go about our business. This

ubiquitous view, however, belies the real impact of standards and conformity assessment – a procedure to verify that products and processes meet a standard – on our economic well being as a nation, as American businesses,

and as world traders in a global economy. Increasingly, standards have become the lingua franca of international trade, and the underlying basis for competition among the world's regions, nations, and corporations large and small. The strategic value of standards, and the participation of American businesses in their development through the private sector voluntary standards process, is fundamental to the well being of our way of life today and will be well into the 21st century.

Several forces have combined in recent years to accelerate the trend to standards and to put standards issues front and center in the national and

**"American companies must understand that standardization is a strategic business issue that has a direct impact on new product development."**



# U.S. Pharmacopeia

*Setting official standards  
of excellence to promote  
the public health*

**F**ounded in 1820, the U.S. Pharmacopeia (USP) is an independent, not-for-profit scientific organization that is responsible for establishing legally recognized product quality standards and authoritative information for the use of medicines and other health care technologies. For more than 175 years, USP's standard-setting activities have contributed to improving the quality of drugs and medical products in the United States.

USP publishes the *U.S. Pharmacopeia* and the *National Formulary* which contain product quality standards for 3,200 drug substances and 250 pharmaceutical ingredients used in making drugs. These standards for medicines are recognized as official by the federal Food, Drug, and Cosmetic Act, and are enforced by the Food and Drug Administration (FDA). The initials "USP" or "NF" on a

international agenda. Domestically, those forces include the proliferation of technology in every domain of life, deregulation, the dramatic political shift in the Congress away from government solutions to those of the private sector, ever rising exports by American industry, and a heightened concern over product quality and occupational safety and health issues in the workplace.

Forces on the international front include intense global competition, the rise of regional trading blocks such as the European Union, the accelerated development of underindustrialized regions from Central Europe to Asia to South America, worldwide concern with environmental issues, and the increased pace and impact of international trade and treaty agreements from NAFTA to the World Trade Organization. Combined, these developments have propelled the issue of standards to center stage.

"As we look to the future, standards will become even more important," says George M.C. Fisher, former CEO of Motorola and Chairman of the U.S. Council of Competitiveness, and now CEO of Eastman Kodak. "American companies must understand that standardization is a strategic business issue that has a direct impact on new product development. There is a direct relationship between leadership in standards and leadership in technology. American standards bodies must lead the way in international activities."

## Standards Defined

A simple definition of the word standard is a recognized unit of comparison by which the correctness of others

can be determined, a set of characteristics or quantities that describes features of a product, process, or service.

As a consumer, buying product that conform to standards makes it easier to comparison shop – for features, functions, and price. This con-

formance not only sharpens competition but provides a basis upon which true differentiation can occur – in features and functions that are valued by the customer – and not in those areas that the customer doesn't see, appreciate, or that add no value to the product's use. More businesses need to focus on customer value analysis. Compatibility standards are especially important and where they exist – such as for stereo equi-

ment interconnection – consumer confidence increases, which translates into increased revenues.

## Reform Efforts

Health care reform is one example where the U.S. is poised for significant government regulatory and procurement changes. There is bipartisan and unanimous support in the area of health care administration including the need to reduce and simplify paperwork. The development of standards related to computer-based patient records is one key component. Another area undergoing dramatic regulatory reform is telecommunications.

Discussions about the global information infrastructure often lose sight of the fact that we already have a national information infrastructure in the broadcast, cable, and phone systems and in a variety of wired and non-wired networks. These link businesses and people in many applica-



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relationship between  
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ship in technology.  
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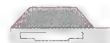
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tions. The issue is the lack of standards that can interconnect these infrastructures and help improve their level of service.

Not surprisingly, the U.S. federal government is the largest creator and user of standards – nearly 52,000 of them. The private sector in America has some 43,000 standards. That's a total of 95,000 standards, which don't include the much larger number of de facto industry standards – such as IBM compatible PCs – that are established not through formal procedures but through widespread acceptance in the free market.

Last year, as part of his acquisition reform efforts, Secretary of Defense William Perry ordered the DoD to look towards the private sector for standards wherever possible. This “dual use” strategy reduces cost, increases the number of supply sources, helps the defense industry convert to commercial market needs, and provides for a more flexible defense industrial capacity.

Says Walter B. Bergmann, II, deputy assistant secretary of defense: “Some analyses project if we adopted private sector standards and specifications we could save between 5 and 10% on weapon costs alone.” The economic benefits – cost displacement from the DoD's perspective, and a single market from the suppliers' perspective – will be welcome to taxpayers and businesses alike.

### Best Practices

American standards have helped promote best practices for much of this century. One recent example: In 1992 Hurricane Andrew ravaged south Florida and Louisiana, damaging or destroying 18,000 mobile homes.

While building codes provide for wind load standards, those standards did not apply to mobile homes, which posed a major public safety issue. As a result, the American Society of Civil Engineers developed a series of stan-

dards subsequently adopted by the U.S. Department of Housing and Urban Development – which sets the standards for mobile homes – so that mobile homes built and sold after July 1994 must resist winds of up to 100 miles per hour in 26 counties in hurricane-prone sections of five states and Puerto Rico.



It is the competitive role of standards, however, that has sparked the interest of nations and businesses. Standards broaden the potential market for goods and services while at the same time providing a basis on which to differentiate products, through cost, time-to-market, quality, and performance. The cooperative partnership between government, industry, and the consumer – one of the best strengths of our market economy – provide the U.S. the best chance for promoting our collective economic welfare and for achieving the common good worldwide.

## World Trade, Government, and the Private Sector

In voting into law the National Competitiveness Act of 1993, the U.S. Congress stated that “strong and effective U.S. leadership and participation in international standards organizations are key to the long-term

competitiveness of U.S. products in global markets,” and called on the federal government to “actively participate in treaty standards organizations and assist private-sector U.S. members of non-treaty international standards organizations in both the development and advancement of technical and policy positions.”

Last year the U.S. exported approximately \$700 billion worth of goods and services worldwide. Twelve million American jobs are directly rela-

to exports, and expanding trade is critical to the economy. The three largest regional markets for U.S. exports are Europe, the Pacific Rim, and Latin America. Together they account for 60% of U.S. exports, with a total of \$300 billion. Of this, \$200 billion is accounted for by the European

**Health care reform is one example where the U.S. is poised for significant government regulatory and procurement changes.**

Union. Standards are fundamental to that trade.

It is no longer sufficient that a product have a large market, be of good quality, and be reasonably priced. Before anything can be traded internationally it must have market access. It's been estimated that an additional \$20 to \$40 billion could be produced by the U.S. if we could overcome all intentional technical barriers to trade – many of which exist only for the protection of domestic markets – and which have been proliferating. Most of these barriers result from disparities in standards and conformity assessment between the U.S. and trading partners.

The intellectual basis for world wide economic cooperation, open markets, and world trade was laid at Bretton Woods in 1944 – the concepts of the International Monetary Fund

## Opening New Markets Worldwide

Hewlett-Packard Company has grown and prospered in recent years — revenues increased \$25 billion last year — without the benefit of central coordination of the company's standards activities. But this is changing, as HP has seen the huge impact of internally proposed standards that in some cases provide little or no benefit to the customer.

**The best standards are those that can generate entirely new markets.**

would have prevented the sale of hundreds of millions of dollars of otherwise safe HP products there. These and similar surprises convinced HP to launch a strategic standards management initiative across the company.

Key to making this happen

was building awareness and sponsorship with

senior management, business units, and geographies around the world — no mean feat in a decentralized culture of 98,000 people producing 23,000 products in 120 coun-

tries. A Standards Strategy Committee was formed last year — staffed from the business and geographic units and chaired by a senior standards person from one of those units — along with a 15 person corporate standards department directly funded by the businesses. They insisted on a contribution to their bottom line. "We have to earn our keep," explains Brian D. Unter, director of corporate external standards. "If we don't deliver value to the HP business units, our department goes away."

HP seeks to gain leverage

and benefit the entire company across product lines. The best standards are those that can generate entirely new markets — such as digital audio tape,



which HP helped develop. Says chairman, president and CEO Lewis E. Platt, "Our contribution to the development of international standards is critical to our goal of manufacturing and selling products to satisfy customer needs worldwide." HP will continue to participate aggressively in standards activities, which it knows contribute to its impressive bottom line performance.

## HOW CAN WE UNLOCK GLOBAL MARKETS?

Infrastructure: Modern roads, bridges, airports, harbors and water systems are essential to worldwide growth.

Designed and built by civil engineers, infrastructure unites trade, creates jobs and wealth, and improves public health and safety.

U.S. economic interests are deeply affected by global infrastructure growth. Emerging markets in Asia, South America and the former Soviet Bloc desperately seek modern infrastructure to attract trade and investment. Global infrastructure renewal thus provides a huge market for U.S. builders and civil engineers.

Emerging markets also will import more U.S. goods and services as infrastructure increases their prosperity.

The good news is that developing nations are investing \$100 billion annually to develop better infrastructure. But for the U.S., the bad news is that many emerging markets use European Union design and construction standards to build their infrastructure.

Such standards erect formidable technical barriers that shut the U.S. out of burgeoning new infrastructure markets. This contributes heavily to America's steady loss of marketshare in overseas construction. Much is at stake: Civil engineering

design and construction comprise America's second largest manufacturing sector, and employ 10 percent of our labor force.

The American Society of Civil Engineers believes the U.S. and world economies will benefit from unified design and construction standards that squarely satisfy all interests—including those of the U.S.

European construction standards often dominate because European governments, building, engineering and standards communities closely cooperate in funding, research and flexing political muscle. By contrast, the U.S. remains largely fragmented. Our clout in harmonizing standards will grow only when our own private and public sectors pull together.

Civil engineers are helping forge that partnership, because they design and build the world's infrastructure. World prosperity depends heavily on modern infrastructure, but infrastructure can achieve its vast potential only if all nations participate in setting standards.

Founded in 1852, the American Society of Civil Engineers represents more than 116,000 civil engineers worldwide. ASCE is a fully accredited standards-developing organization, and a founding organizational member of the American National Standards Institute.





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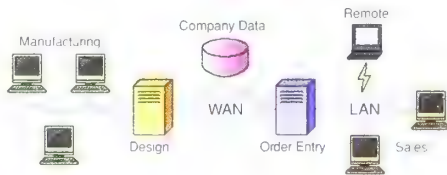
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**There are only two kinds of organizations: those that have embraced the global standards process, and those that will.**

t where governments and trad-locks can distort the playing field through standards – erect trade s that thwart the intent of agreements.

consider this recent comment by Hermann Franz, chairman of ns' supervisory board: "Europe et standards worldwide just d in the past. We must take ot to allow other countries and s to set international standards ereby preempt the markets mselves. European standard- is a tool for creating competi- vantage... and should come minate the contents of interna- standards."

ANIST

U.S., the American National rds Institute (ANSI) – a pri- onprofit membership organiza- coordinates the U.S. voluntary rds system bringing together vate and public sectors to p standards for a wide array of industries. Founded in 1918, the te's membership today includes corporations, 39 government es, and 289 other organizations. e official representative to the ational Organization for Stan- ation (ISO), the International otechnical Commission, and egiional standards bodies. does not develop standards ut ensures that consensus, due s, and openness – along with ocedures – are followed by ds of standards development

organizations as they establish stan- dards for their respective industries. Many of these are subsequently

adopted as American National Standards, currently 11,500 of them.

Ensuring the integrity of the U.S. voluntary standards system is the most important aspect of the ANSI mission to enhance

U.S. global competitiveness and quality of life. "ANSI's value is as an effective coordinator of American standards policy, the accreditation of standards developers, and as a vital standards information resource," explains Sergio Mazza, ANSI president since 1993 and former president of Memorex U.S.A. "The U.S. voluntary consensus standards community represented by ANSI comprises a unique American system: diverse membership, an open and published process, opportunities for public

## Global Advantage & Positioning

**W**ith \$128.4 billion in revenues and nearly 340,000 employees in 34 countries, few businesses can equal the reach of Ford Motor Company, the world's biggest producer of trucks and the second largest producer of cars and trucks combined. Early this year, Ford U.S. and Ford Europe became Ford Automotive Operations with single, centralized departments and processes. The need to grow drove the decision to transform. More than 80% of the world's population live outside Ford's traditional markets. Ford believes global standards are key to reaching those potential customers.



With one billion people, China represents a vast potential auto market. But what are the customary standards, even those as basic as

human body sizes and proportions? What is the voice of the customer in a formerly command economy? Highway infrastructure, fuel quality and availability, and many other factors – taken for granted in the West – have yet to be fully determined.

Ford is committed to using standards to eliminate non-value added differences in its products, and to differentiate itself from the competition. It seeks to eliminate costly redundancy and recertification

often required by governments, seeking one standard, one conformance test, one accreditation, and one recognition.

By standardizing on less than 20 of some 130

possible coatings on thousands of bolt types, Ford is saving millions of dollars. But it didn't stop there. It developed a now-patented bolt that can't be cross-threaded when inserted by machines – a new performance standard for Ford – eliminating other bolts

**Ford is committed to using standards to eliminate non-value added differences in its products.**

and dramatically increasing quality and productivity. "Standards development at Ford has become a competitive venture, fast paced, intellectually demanding, results oriented, and global," explains Keith Termaat, strategic standardization manager. "Setting high standards is an essential principle – high standards for ourselves, for our company, and for our customers."





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due process and a cooperative relationship with federal, state and local regulating bodies," said the Hon. Robert S. Walker (R-Calif.), chairman of the Committee on Commerce in the U.S. House of Representatives. "It is a perfect testament to the genius of our economic and regulatory systems. Its success is mirrored in the high level of acceptance and credibility that voluntary standards have been accorded in our country and in the international arena, and the support of our regulatory agencies of government."

Within the federal government, the primary responsibility for coordinating the technological basis for standards that help accomplish this rests with the National Institute of Standards and Technology (NIST) – an agency of the U.S. Commerce Department – which promotes economic growth by working with industry to apply technology,



**As a consumer,  
buying products that  
conform to standards  
makes it easier to comparison shop.**

measurement, and standards through a focus on the nation's technology infrastructure. The inherent value of

infrastructure and measurement is that it is freely and equally available to all. We take it for granted that

when we pump a gallon of gas at the gas station, we get a real gallon, and that remains true anywhere in the country. The measurement system for this traces back to NIST.

NIST works with industry and the rest of the U.S. sector to facilitate the private voluntary standards process. An important step in reinforcing such partnerships occurred in July of this year, when NIST signed a memorandum of understanding with ANSI to enhance and strengthen the national voluntary standards system. "Both NIST and ANSI agree on the need for a national approach to develop the best possible international standards to strengthen U.S. competitiveness," explains Dr. Arati Prabhakar, NIST director. Both organizations saw the need for a national strategy – not just a federal one – at the international standards negotiating table, as well as the need for an appropriate balance between the voluntary, open, consensus-based standards setting process and government regulation, especially in health and safety areas. In fact, NIST supports the federal government's continuing movement away from regulations to reliance on voluntary standards. The intent of the NIST-ANSI agreement is to serve as an anchor for the whole voluntary standards system, to better coordinate that system with the work of the federal government, and to boost the voice of the U.S. private standards system in international negotiations, helping to maximize the benefit back to the U.S.

## Advocacy, Innovation & Performance

AMP Inc. is the world leader in electrical/electronic connection devices, found in everything from automobiles to computers to washing machines. More than 100 million of AMP's more than 100 billion in revenue is derived

**AMP**

from products that conform to industry standards. But don't equate standards with a lack of product innovation: In 1998, AMP received 100 patents, among the top 25 U.S. corporations. Standards are a market-driven phenomenon that precede many innovative products that they describe – sometimes creating new markets in the process – and become the baseline on which real value differentiation can occur. Few companies have been as articulate or as successful as AMP in contributing to the national dialogue on the value of

standards in competing globally as a nation, whether it be testifying before Congress or advising the U.S. Trade Representative. Educating U.S. business executives on the importance of standards in world trade – and encouraging

them to be advocates for American interests in the international arena – may be even more important. Says William J. Hudson, President and CEO: "Companies taking an aggressive approach to standards can derive a critical competitive advantage in shorter time-to-market and a higher 'hit' ratio, while those that adopt a defensive posture of simply creating products that conform to existing standards risk falling behind

on the learning curve."

AMP's internal standards training program is recognized as a "best practice" model, and served as a basis for ANSI's own national education and training program. Education begins and ends from the customers' perspective. It is not by accident that AMP's Global Products Standards department reports to the corporate vice president of Global

**Standards are a market-driven phenomenon that precede many innovative products.**

Marketing. Adds Henry Line, who heads the department: "Standards are not an end in themselves. They must be part of the company's global market strategy and the new product development efforts demanded by our customers' requirements."



## U.S. Product Data Association Makes It Happen

**F**uture U.S. industrial competitiveness depends on the development and application of new information technology standards that are being required by the international marketplace.

The International Standard for the Exchange of Product Model Data (STEP), currently under development, is the most compre-

hensive information technology standard

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developed to date for 21st century manufacturing. Today, the U.S. Product Data Association (US PRO) leads the development of this standard in both the national and international arenas.

STEP will not only change the way we design, produce and support products, it will change the way we do business.

US PRO, through its IGES/PDES Organization, is the ANSI-accredited organization for the development of standards for the exchange and sharing of product information.

When it comes to STEP, industries worldwide can make it happen, watch it happen, or wonder what happened. U.S. industry, through US PRO, is making it happen.

U.S. Product Data Association  
2722 Merrilee Drive, Suite 200  
Fairfax, VA 22031

Phone: 703-698-9606

FAX: 703-560-2752

E-mail: [uspro@uspro.fairfax.va.us](mailto:uspro@uspro.fairfax.va.us)

### Conformance and Quality

Traders in the world market must be prepared to satisfy two conditions to enter global competition: assurance that the products or services conform to the standards of the receiving market, and proof of a quality management system for products, services, and operations. U.S. standards systems must be recognized by our trading partners in NAFTA, the European Union, the Market of the Americas, and the Asia-Pacific Economic Cooperation if we are to achieve the goal of "one product, tested once, sold worldwide." The U.S. does not want to be on the receiving end of a surprise again – as it was with ISO 9000 – where European forces drove the agenda.

As a matter of national policy, we want to eliminate what U.S. Trade Representative Mickey Kantor calls "sanctuary economies." Says Kantor: "We will insist that the United States have the same access to foreign markets as foreign countries have to our markets. We can't engage in a level playing field, equal trade, open up markets and get rid of trade barriers unless we harmonize standards."

Motorola's president and CEO Gary Tooker states: "To a large degree, the success of voluntary industry standards will determine whether American products and services can survive in the intense competition of the global marketplace." Agrees Prabhakar: "The strategic value of standards to the national economy is beyond doubt, and the pace of development of international standards is accelerating. What isn't clear is whether we, or someone else, will get the economic advantage. Active participation by American business in the standards process in a strategic sense is critical to ensuring that we secure that advantage."

## U.S. Voluntary Standards and Conformity Assessment

**V**oluntary standards – open standards developed by consensus and due process in the private sector – provide an essential framework (some would argue they should provide only a minimal framework), leaving the maximum possible room for innovation which companies can add value, differentiate themselves, and compete. Standards enable innovation, remove barriers, and facilitate the flow of information, products, and services between customers and suppliers.

While there is no single international or national process for developing standards, those that arise from a formal, coordinated, consensus-based and open process by interested parties – commonly called voluntary consensus standards – are at the heart of the U.S. system. De facto or market standards do not always ensure a level playing field. Proprietary solutions to market needs often do not lead to optimal economic benefit for the entire



**"Active participation by American business in the standards process in a strategic sense is critical to ensuring that we secure [the] advantage."**

economic system. Because standardization requires gathering data and making comparisons

among the needs of diverse stakeholders, cooperation by all parties is required. When this due process is followed, the standards that result provide economic benefit – including compatibility and economy of scale – to the many, rather than the few.

### Standards Developers

In the U.S., there are more than 40 private standards developers. Standards development organizations (SDOs) are the core of the decentralized voluntary standards development process in the U.S. Most of the



by open consensus and due to their respective subject domains are accredited by American National Standards Institute (ANSI). One of the largest standards development organizations is ASTM, American Society for Testing and Materials, with nearly 10,000 standards recognized and used the world over. These cover fields from metals, chemical services, and building construction to environmental management, plastics, and petroleum. Another well recognized SDO is Underwriters Laboratories (UL), which provides product safety certification programs to ensure that products meet internationally recognized safety standards. Others include the Society of Automotive Engineers (SAE) – whose best known standards include motor oil viscosity ratings SAE 10W-30 and 10W-40 and the National Fire Protection Association (NFPA) – whose performance standards for sprinkler systems are used worldwide.

#### Conformity Assessment

Conformity assessment is the term used to describe steps taken by both manufacturers and independent third parties to assess conformance to standards. A manufacturer's declaration of conformity is one method of achieving this. This is favored by many larger companies with sophisticated and established internal testing and

quality assurance systems and for whom an independent third party review seems unnecessary and expensive at best. The other approach is a third party assessment based on a

**Standards enable innovation, remove barriers, and facilitate the flow of information, products, and services between customers and suppliers.**

determination that a product conforms to a particular standard. This assessment often functions as a seal of approval that can increase buyers' confidence that the product actually conforms to a claimed standard. Third party assessment can take the form of product testing (by an independent laboratory), certification (against some standard), or registration (e.g., ISO 9000 by a quality systems registrar).

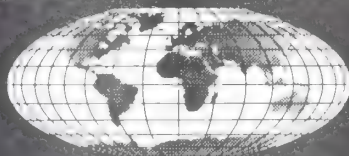
Third party conformity assessment has been growing in the U.S. It is estimated that there are some 5,500 independent, for-profit testing laboratories alone, double the amount from ten years ago. Certification is a form of third party conformity assessment – usually a certification mark – that stipulates a product performs to specified requirements. Underwriters Laboratories (UL) and the American Dental Association are good examples of certifiers, on electrical devices and toothpaste respectively. For many consumers, these "listings" and marks provide reassurance that the product they are buying is either healthy, safe, or both, and conforms to the accepted standard.

The biggest growth in the conformance business has come with the rapid proliferation of registration for quality management systems, which has for some time been promoted by the European Union. The International Organization for Standardization (ISO) 9000 quality system standards are perhaps the best known. In



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the eight years since its introduction, the number of ISO 9000 registered U.S. firms has grown to 3,500. The cost of such registration – which begins with the initial registration and continues with a periodic follow-up audit – is high. The standards require manufacturers to document their production processes and develop means to improve them – but they are no guarantee of quality products. Rather, the focus is on the process of delivering a product of consistent quality – whatever that quality is.

The real problem with quality system registration is its spiraling cost and redundancy. This places a serious burden on U.S. suppliers, who are increasingly required by either the government or other manufacturers or both to have their quality systems registered by third parties. Because multi-national mutual recognition



**The integrity of the U.S. voluntary standards system is the most important aspect of the ANSI mission.**

agreements are not yet in place, they are costly, duplicative, and multiple registrations. ANSI is leading U.S. negotiations on both a bi-lateral and

multi-lateral basis to achieve one-time registration that will be accepted

a global basis.

Companies who successfully propose their technology as the basis of an industry-accepted standard avoid being relegated to an otherwise proprietary and smaller niche market ahead on the competitive learning curve for that technology, and may also benefit from royalties from other users. Says ANSI's Mazza: "The message to American industry is to get involved. When you're not at the table, you can't participate effectively and you'll have little or no chance of proposing your own technology as the basis of a national or international standard. It costs relatively little to contribute to the voluntary standard process, and the rewards can be enormous."

## Industry Leadership & Time to Market

**W**ith \$64 billion in revenues and 219,000 employees worldwide, IBM markets thousands of products from semiconductors to software to mainframe computers in more than 159 countries. "IBM's customers are demanding open, interoperable systems, and the way to achieve that is through standards," according to Lawrence L. Wills, IBM's director of standards. Defining what standards are of interest to the company and being involved in external standards activities is the responsibility of the divisions and geographies, who at any given time collectively field 400 to 800 individuals (part-time).

The cost is insignificant as compared to the benefits. "If you're not at the table participating, you

don't have a voice in what's happening," says Wills – who is also Chairman of ANSI – "and you are in effect letting your competition define what your products are going to look like in the future."

Active participation in standards activities permits IBM to get its own technologies into the process, better understand where the standards are going, and help facilitate speed to market. An international standard permits IBM to build one product and market it worldwide. Standards and how they

are used in products are an integral, increasingly

formalized part of the company's general management and strategic planning process.

In an information

technology (IT) industry where historical 4 to 6 year product life cycles have been reduced in some instances to 12 to 18 months, IBM's challenge is to ensure a more responsive process and compress the time it takes to get standards approved. International IT standards are being

**"If you're not at the table participating, you don't have a voice in what's happening."**

developed in less than 30 months and approaching 24 months but are still not aligned with the fast product cycles that are the hallmark of today's IT industry. IBM's participation in standards bodies helps ensure that the development and approval procedures put in place are necessary and value-added to both industry and itself.

**IBM**

## Environmental Management

**A**nother major standards development effort with profound consequences for industry worldwide is the proposed ISO 14000 Environmental Management Systems standard. In 1991, the U.N. asked the ISO to develop a management process to help safeguard the environment to enact global standards for environmental management systems and auditing tools, from auditing to life cycle assessment.

The business case was simple: growing worldwide desire by nations and people for better risk management and improvement in how to manage the environment. A truly

# What Do the Best Companies Say?

say "we have the best project managers." According to research published in the *Harvard Business Review*, the companies consistently attribute their success to their project managers. To project managers who know how to manage projects and how to stay close to the customer. To project managers who get better results to more markets faster. Maybe that's why a leading business publication recently labeled Project Management #1.

**What is a Project?** A project is a temporary endeavor undertaken to create a unique product or service. Examples of projects include: developing a new product, developing a new information system, constructing a building, and launching a new business process. Projects are undertaken at all levels of the organization and can involve a single person or many thousands. The project manager applies knowledge, skills, tools and techniques in order to meet or exceed customer needs and expectations.

**Can Your Organization Improve Project Performance?** One way is to use the standards defined by the Project Management Institute (PMI) in its publication *A Guide to the Project Management Body of Knowledge (PMBOK)*.

**Senior management views project management as an essential element in our drive toward technical excellence. Our aerospace organization has adopted the PMBOK Guide as a standard framework for project management."**

Chuck Schmidt, Allied Signal, Director, Center for Process Improvement

The *PMBOK Guide* provides a basic reference for anyone interested in the profession of project management. It is also used to provide a consistent structure for professional development programs:

Certification of Project Management Professionals (PMPs) and accreditation of degree-granting educational programs in project management.

TASC, Inc., a company in the information technology business and a strong advocate of project management standards, states its investments in project management infrastructure, processes, and professional certification training, all pay dividends.

**What are Project Management Standards?** The *Project Management Body of Knowledge (PMBOK)* is an inclusive term that describes the sum of knowledge within the profession. As with other professions such as law, medicine, and accounting, the body of knowledge rests with the practitioners and academics who apply and advance it.

The *PMBOK* includes knowledge of proven, traditional practices which are widely applied as well as knowledge of innovative and advanced ones which have seen more limited use.

**"Project management standards give our employees the knowledge base to build upon and be prepared for the dynamic business environment of the future."**

R.L. Eastman, AT&T, Director Government Programs

PMI's *PMBOK Guide* identifies and describes that subset of the *PMBOK* which is *generally accepted*. Generally accepted means that the knowledge and practices described are applicable to most projects most of the time, and that there is widespread consensus about their value and usefulness.

Generally accepted does *not* mean that these practices are, or should be, applied uniformly on all projects; the project management team is always responsible for determining what is appropriate for any given project.

**Organizations Using Project Management to Achieve Corporate Objectives** A highly competitive global marketplace demands that businesses get new projects and business development completed quickly, on-time and within budget. William R. Duncan, PMP, a partner at Duncan-Nevison in Lexington, MA and PMI's Director of Standards, notes that Camp Dresser & McKee Inc. (CDM) has developed its project management process using the *PMBOK Guide*. CDM uses this process to accelerate the schedule and reduce the budget on its environmental engineering projects without compromising its strict quality standards.

From high-tech to insurance, Fortune 1000 to small business, project management is fueling much of the successful development of exciting new business enterprises.

**"A repeatable project management process provides consistent and effective control of projects enabling us to better meet our customer requirements for information technology services."**

Tom Block, EDS Project Management Consulting

**What Does the Future Hold?** Project management leadership has become a highly sought-after skill applicable at every level of an organization. The standards setting activities of volunteers from the profession are making it possible for organizations to prepare for the higher demands of the future.

PMI, a non-profit professional association located in Upper Darby, Pennsylvania, represents members worldwide who are actively advancing the project management profession.

**For more information, contact PMI:**  
130 South State Road, Upper Darby,  
PA 19082. Tel: (610) 734-3330  
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are made possible through the generous contributions of these leading edge organizations who employ and advocate project management principles and standards.

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Superhighway  
or country road?

# Standards will make the difference.

Much has been said about the information superhighway. How it will change the way people around the world find and exchange information and ideas. How it will be an engine for growth, learning and commerce. How it will allow us all to connect at a higher level. ♦ Standards play an important part in paving this highway. Making sure that competing protocols and specifications don't become major roadblocks and slow it to a crawl. ♦ AMP is proud to play a part in the creation of the global information superhighway. Proud of our over 36,000 people worldwide, who are providing the physical pieces (from connectors, cables and switches all the way to wireless systems) and those participating in the development of the standards that will help it reach its true potential.

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**HIGHER**  
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ional effort, such as this, would  
empt potentially conflicting and  
ore costly national or regional  
ons and standards, which were  
beginning to emerge.

In 1993 the ISO 14000 technical  
ce, and dozens of subcommit-  
their working groups, have  
hundreds of times to discuss and  
a framework to address envi-  
mental issues. The U.S., which has  
ple involved, is represented by

Unlike the devel-  
of ISO 9000 –  
uch of American  
was asleep at  
ch – America has  
ively involved at  
e from day one.

Cascio, who  
e U.S. Technical  
y Group for ISO  
nd is IBM's pro-  
ector for envi-  
mental health and  
standardization:  
S. industry not  
proactive this  
und, we might  
e precluded the  
n the part of  
Europeans from

enting a performance, vs. a  
standard, which would have  
ely instituted European regula-  
nd technologies – for specific  
emissions and pollution that  
ve been in conflict with our  
ional interests. In essence, it  
ave created an effective trade

ISO 9000, ISO 14000 is a  
process management stan-  
not performance or quality  
s. Neither are concerned with  
quality itself – which is the  
of the manufacturer and its  
rs – but rather with the con-  
of quality. ISO 9000 certifica-  
example, is a guarantee that  
turers are consistent in the  
that they follow. This means

written process procedures, consistent-  
ly executed, that are both communi-  
cated to and understood by employees  
and customers alike.

Many in American industry – if  
they are aware of ISO 14000 at all –  
are concerned about its costs. These  
include not just the cost of initial com-  
pliance and registration, but the ongo-  
ing costs of maintaining that certifica-  
tion (or registration by a third party).  
If the experience of ISO 9000 is any

indicator, ISO 14000  
will indeed be very  
expensive, though many  
experts calculate the  
cost at only half of the  
expense of ISO 9000  
registration. For large  
companies, that trans-  
lates into anywhere  
from \$100,000 to \$1 mil-  
lion per plant.

Consider, however,  
the alternative: trade-  
restrictive and regional-  
ly-unique performance  
standards vs. prescrip-  
tive standards and frag-  
mented, uneven compli-  
ance and enforcement  
mechanisms that –

besides being a management  
headache of the first order – could  
triple the cost of implementation.  
When seen against the backdrop of  
ISO 9000 – when U.S. industry was  
largely absent from the table, the ISO  
14000 process has worked compara-  
tively well for us.

Smart companies will get involved  
to ensure that this remains the case,  
and will anticipate the impact of and  
prepare themselves for these environ-  
mental management standards. The  
Environmental Protection Agency  
sees ISO 14000 as a vehicle for joint  
industry-government efforts in finding  
effective voluntary approaches in  
achieving compliance. The most inno-  
vative among us will also find creative  
ways to use ISO 14000 compliance to



**Companies who  
successfully propose  
their technology as  
the basis for an  
industry-accepted  
standard...are ahead  
on the competitive  
learning curve for  
that technology.**

## ISA Standards Impact Your Business Globally

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within ISA span nearly every  
industry and ISA. They are essen-  
tial to the manufacture of prod-  
ucts from cosmetics to cars. Envi-  
ronmental emissions control, qual-  
ity control, efficient use of energy,  
reduced waste...all rely on mea-  
surement and control technolo-  
gies; all are vital to global competi-  
tiveness. ISA is The International  
Society of Measurement and Con-  
trol, with 49,000 members in 80  
countries. For 20 years, ISA has  
been accredited as an ANSI-recog-  
nized standards writing body. And  
for over 10 years, we have held IEC  
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tional electrical standards.

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## Nortel Committed to Voluntary Standards

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Nortel and its R&D subsidiary, BNR, are committed to the development of timely, open, public, voluntary standards that promote the growth and competitiveness of the worldwide telecommunications and information technology industries.

Accordingly, we actively participate in the key telecommunications and information technology standards committees in ANSI, the ITU and ISO/IEC, with the objective of fostering growth in global markets.

We strongly support partnering

between  
newly  
formed  
industry

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consortia and forums, such as the ATM Forum and the traditional, accredited standards bodies, to assure that a single set of high-quality interoperability specifications is developed to support the rapid deployment of new technologies in the competitive marketplace.

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demonstrate to customers that – when it comes to the environment and safety – they are well managed and good corporate citizens. As we approach the end of the millennium, businesses will find that being “green” is just good business.

## Strategic Standardization and Enlightened Self Interest

**O**ne of the most successful American exports has been software, and Japan has been a crown jewel for us in that regard – \$2.7 billion in 1994 alone. Until last month, there was widespread concern that Japan's Ministry of International Trade and Industry (MITI) would require that foreign-made software be certified by the unique standards of the Japan Accreditation Board (JAB). Because they alone can perform the conformity assessment tests and certify that products meet their standard, the reasoning went, the Japanese are in a position to gain access to our software expertise.

Fortunately, this concern has been allayed. The U.S. – led by the private and public representatives of ANSI – has successfully concluded an agreement on the role of international standards and established a common set of principles and procedures to guide the development of conformity assessment approaches for software sales in Japan.

In wireless digital communications, the Europeans pulled ahead with their Groupe Speciale Mobile (GSM) standard. Until recently, U.S. cellular companies were still quibbling over competing digital standards. While not the only reason Europe is ahead – they don't have the drag of the huge U.S.

analog infrastructure – with the geometric growth curve of digital cellular customers in Europe (a 10 to 1 ratio over the U.S.), the GSM standard dominated the wireless world. Because U.S. industry could not develop a consensus position, European providers were poised for a windfall. Now, however, U.S. manufacturers are playing a leading role in the next level of frequency bands which will help gain a stronger global position for U.S. products.

Examples such as these under-



**The focus is  
on the process  
of delivering  
a product  
of consistent  
quality.**

the importance that standards can have as technical barriers to trade – by means unique to Japan and Europe – and serve as a clarion call that the price of free and open world markets requires more than government-initiated trade agreements. For American business, it requires the commitment and active participation in the U.S. voluntary standards system – the only one in the world – business helping business out of enlightened self interest.

The most enlightened corporations have established strategic standardization programs to ensure that a standards policy is an integral part of corporate and business strategy, not just among large corporations. As a medium-size company, we simply had to get involved in the process of trying to influence the writing of standards, and of understanding what issues really are,” explains J. Hartmann Kluge, chairman of Automatic Systems Co. “If you are not involved in standards or standards-setting, you will

side and the competition will pay with your business." William Hill, executive vice president and chief financial officer of Polaroid said, "Strategic standardization is a mental dimension of our corporate strategy without which we could not grow our global market share." He might add that in the wealth of the world today, there are only two types of organizations: those who have embraced the global standards

process, and those that will.

*Written by Robert L. Howie, Jr., vice president of International Systems Services Corporation (ISS), which partners with clients worldwide to deliver business results through change mobilization and information technology. 1.800.DIAL ISS or rhowie@800.dialiss.com*



Design and art direction by Shostak Studios, Inc., New York.

## Refining Product & Service Delivery

Ameritech keeps 13 million customers in touch through telephones, cellular, paging, video, and information networks. Some 100 employees of Baby Bell helped generate \$12.6 billion in revenues last year.

Ameritech wants to reduce customers' uncertainty that a new product or service will interoperate with their existing ones and be compatible with their lifestyle. In voice messaging, business, wireless, and residential customers each employ dif-

ferent codes to perform the same function. A set of common codes would reduce confusion. Determining early the right standards to use can accelerate the adoption of new products sooner. The lack until recently of a commonly accepted signaling standard for screen phones, for example, delayed their successful introduction. Once a standard was agreed upon – the Analog Dis-

play Services Interface (ADSI) – manufacturers could be assured enough market volume to produce screen phones that could retail for under \$200.00 – a condition for widespread consumer acceptance.

Explains Michael G. Gorman, who oversees standards for the company, "We've moved from viewing standards as a technical concern to seeing them as a basic customer and marketing issue. If we can involve end users in standards development – in the process making the standards more accepted by manufacturers – we can increase American competitive advantage." Ameritech –

**Ameritech**

through its active participation in national standards development policy – is seeking to do just that.

**Determining early the right standards to use can accelerate the adoption of new products.**

ferent codes to perform the same function. A set of common codes would reduce confusion. Determining early the right standards to use can accelerate the adoption of new products sooner. The lack until recently of a commonly accepted signaling standard for screen phones, for example, delayed their successful introduction. Once a standard was agreed upon – the Analog Dis-

## ARE YOUR COMPETITORS STACKING THE DECK?



If you are not treating standards as a management tool, you may be giving your competition the opportunity to set the rules at your expense. By not participating in the U.S. voluntary standards system, you allow competitors to influence business issues and gain an edge.

Your option is to become involved by joining other leading U.S. businesses, organizations, and government bodies in the ANSI Federation. As an ANSI member, you can help influence domestic and international policy on standards and trade issues. You can compare how your company manages standardization with some of the "best in class". You can stay informed on future trends that impact your business.

Get involved today and network with leaders in business and industry tomorrow. For more information, contact:

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# QUALITY IS JOB 1

# THE RUGRATS' REAL MOM AND DAD

ky and Csupo bring high style to TV cartoons

When Arlene Klasky and Gabor Csupo met, it was a fluke. It was 1979, and Klasky, a graphic designer from California, vacationing in Sweden. Csupo, a Hungarian-born animator, had made his home in Los Angeles after fleeing communism in 1975 by walking for two and a half hours through a tunnel from Yugoslavia to Austria. The pair soon married and moved to Los Angeles, and in 1982 founded an animation and graphic design company, Klasky Csupo Inc., in a room of their home.

Though they're now ending their marriage, having filed for divorce in 1991, the pair's professional collabora-

tion is stronger than ever. Their Hollywood studio today employs more than 200, is animating three TV shows, working on a movie deal, and pumping out animated ads. Another Klasky Csupo creation, *Rugrats*, is the No. 1 cable kids' show. Credit in part an unprecedented wave of growth in demand. "The amount of animation done in the golden age of animation was insignificant compared to what's being done now," says Harvey Deneroff, editor of *The Animation Report*, an industry newsletter. Says Klasky: "Were we ever in the right place at the right time."

Credit also goes to the duo's distinctive look—loose, hip, high-quality ani-

mation. Their break came in 1988, when the studio was hired to animate one-minute shorts of *The Simpsons*. While *Simpsons* creator Matt Groening controlled tone and style, it was Klasky Csupo that made Bart Simpson's skin yellow and Marge's coif blue.

**"HOUSE STYLE."** After *The Simpsons* became a series, Klasky Csupo animated it for three seasons. About the same time, the couple, who by then had two sons, submitted an idea to Viacom Inc.'s Nickelodeon, which was on a \$40 million campaign to create original animation. The idea—for a show depicting the world as experienced by babies—became *Rugrats*, a three-time Emmy winner. A second Nickelodeon show, *AAAH!! Real Monsters*, now in its second season, further established the studio's offbeat, irreverent approach. "They have a house style," says Linda Simensky, an animation executive. "Whatever they do, you can tell it's them."

That style, Csupo boasts, has "conquered television." Now 43, he looks thoroughly Californian: His standard office wear is shorts, open shirt, and one glittering earring. But his eye remains international. The studio's staff ranges from recent U.S. art-school grads to animators who worked a near-lifetime in Russia. "Gabor just has very good taste," says Joe Ansolabehere, a writer on *Rugrats* and other Klasky Csupo projects. "He has the ability to find talent-

## THE FOLKS WHO MADE THE SIMPSON YELLOW

animating the first three seasons of *Simpsons*, Arlene Klasky and Gabor Csupo have launched a string of animated creations:

**RUGRATS** Now in its fifth year on Nickelodeon, this baby's-eye view of the world has won three Emmys.

**AAAH!! REAL MONSTERS** Beginning its second season on Nickelodeon.

**THE KRAMERS** Strictly for adults, the adventures of the foul-mouthed private investigators are the cornerstone of Nickelodeon's image-changing Saturday night lineup.

**THE BUGS** The duo's first Saturday morning network cartoon, which premiered in 1991 on CBS. For the time, they own licensing rights.





# HOT TRANSCRIPTS

Missed the chance to talk with Netscape co-founder **Marc Andreessen** when he was the guest of a Business Week Online live conference? Or maybe you were away when BW economist **Bill Wolman** gave his latest investment advice.

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How to navigate in this sizzling market, with John Levinson of Lynch & Mayer—8/21/95

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## People

ed people and use them better than anyone I know."

Klasky, for her part, concentrates on story lines. And despite *Rugrats*' slightly subversive tone—the overbearing character Charlotte, cell phone glued to her ear, is enough to put any working mom's teeth on edge—she is firm about her desire to "do something ever so slightly educational" for kids. Indeed, last year's Passover episode—in which diapered protagonist Tommy intoned "Let my babies go!"—garnered a review in *The New York Times*. While much of *Santo Bugito*, the studio's new CBS Saturday morning show, is given over to bug-centered humor, Klasky is proud of periodic intrusions by the Professor, a clipboard-toting purveyor of the odd educational fact.

**QUIRKY TASTE.** As a working mom herself, Klasky describes her typical day as: "exercise, kids, work, pick the kids up from school, homework, fax machine, phone calls, reading all the scripts, and talking to our CEO and executives at night after the kids are in bed." Brandon, 7, and Jarrett, 10, have inspired much of their parents' work. During a vacation at a Mexican Club Med, Klasky says, Brandon became mad about mariachi music. One result is the Latin sound of *Santo Bugito*. Inspiration also comes from collaborators' kids: *Rugrats*' Tommy is named after the son of producer Paul Germain, who oversaw that show's first three seasons.

Csupo's quirky taste has at times been a tough sell. He shopped around an idea based on the underground comic *Duckman* for a year before financing the \$400,000 pilot himself. After the pilot was enthusiastically received at European animation festivals, Viacom's Paramount Domestic Television decided to finance the show. One of the few animated series for adults, *Duckman* is a spoof of the likes of Daffy and Donald Duck—a cursing, cigar-smoking private eye. Rod Perth, president of USA Networks Entertainment, which has made *Duckman* the cornerstone of its upcoming Saturday night comedy lineup, calls the series "critical" to the channel's search for a look that stands out in the cable crowd.

While Klasky Csupo is privately held and does not disclose revenues or profits, this year's slate of animation production—26 episodes of *AAAH!! Real Monsters*, 22 of *Duckman*, and 13 of *Santo Bugito*—alone should generate more than \$21 million in revenue for the studio. Profitable since it won *The Simpsons* in 1988, the company gets more than 10% of its revenues from products other than animated series,

such as commercials and rock videos.

*Santo Bugito* could mark a big step through for the studio. Earlier shows were owned outright by Nickelodeon and Paramount. But *Santo Bugito* is financed half by CBS Inc. and half by European investors, is the first produced by Klasky Csupo owns. That gives the entry into the potentially lucrative world of merchandising. Soon to hit stores are *Santo Bugito* ant farms, T-shirts, and stickers—all paying an average rate of 10% to the studio, which will give over half to a licensing firm.

Now under discussion is the studio's first full-length feature film; the runner seems to be a *Rugrats* production by Paramount. It is ironic even as Klasky and Csupo stand on the brink of their biggest successes that they are ending their 16-year marriage. While neither would discuss their relationship,

**A Klasky day:**  
"Exercise, kids, work,  
pick the kids up from  
school, homework."

up, present and former colleagues haven't affected their work and the two generally handle different parts of the business.

What may affect their work, says some former employees, is an increased emphasis on business issues as the studio has grown. Klasky and Csupo say they're as focused as ever on creative work. That's an important image to maintain given the exploding demand for talented animators. Theatrical successes such as *The Lion King*, which earned Paramount an estimated \$600 million, have given major motion picture studio ramping a slate of animated features. Fox Broadcasting Co., WB Network, and other groups are featuring animation in seven days a week, and CD-ROM manufacturers are adding to demand.

Others in the industry agree that success hasn't spoiled Klasky and Csupo. "It's nice to see artists running the studio," says John Kricfalusi, creator of Nickelodeon's first animated smash, *Ren & Stimpy Show*. Howard Beal, *Rugrats* director, also likes seeing Klasky in charge. Csupo, he says, "would rather close his doors than create drama; that policy seems to be paying off beautifully."

By Nanette Byrnes in Hollywood

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EDITED BY AMY DUNKIN

## HOME SWEET MOVIE PALACE

**Y**ou've got the night off, and you'd love to escape into a good movie. You want that big-screen experience and those special effects that make you feel like you're surrounded by the action. But when you consult the local movie guide, nothing fits the bill, or the times don't work. Or maybe you just don't want to share the same space with a bunch of noisy teenagers.

This is the moment when a home theater starts making sense. The amount of entertainment available to you in the home is staggering. There's cable and broadcast TV as well as the entire inventory of your local video store. If you want to invest about \$700 for a dish, you can obtain your programming directly from space via one of the new digital satellite systems—getting the best picture and sound available. Couple any of those choices with modern video and audio technology, and you can reproduce the sensations of a real theater without breaking the bank.

**TRIPLE PLAY.** The idea of building a home theater may seem daunting at first. After all, some video fanatics have even tacked on media rooms to their houses. But nobody is asking you to replicate Radio City. Generally speaking, you should be able to fit all the components required into an average living room or den.

While true believers can watch costs soar into five figures, you can assemble a de-

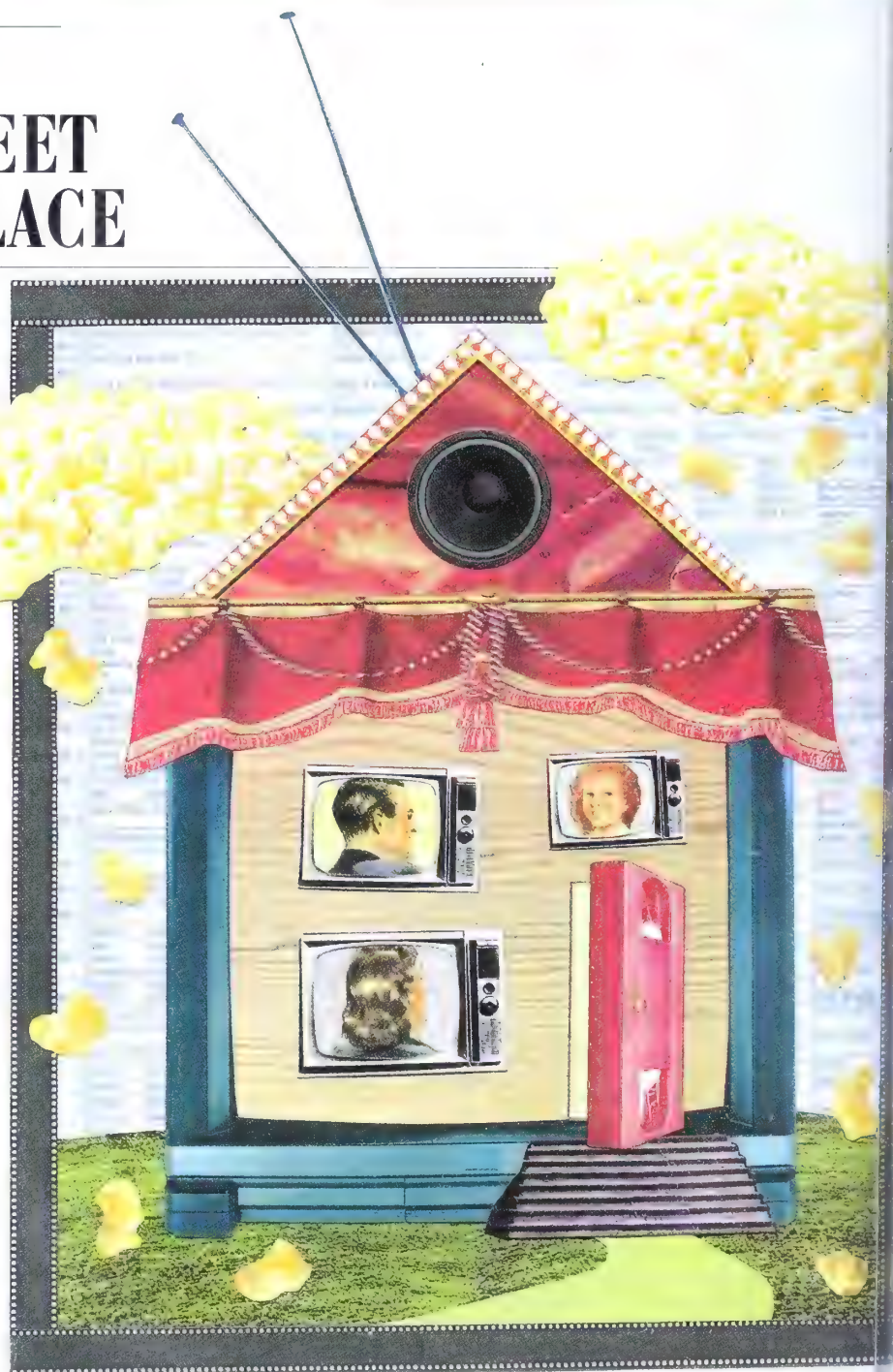
cent system for a fraction of that. You already may have some of the necessary equipment, such as a TV or stereo receiver. If so, then it may only be a matter of adding one or two elements, such as extra speakers—which can be done for as little as \$1,000. If you need

a larger-screen TV plus some other pieces, expect to spend \$1,500 to \$5,000.

The best way to approach the idea of a home theater is to break it down into three parts: source, screen, and sound. Consider the source. Nearly everyone has a videocassette recorder. But for home theater, you'll need a hi-fi VCR, which by definition

has separate outputs for video and left and right channels for stereo sound.

Another video source is the laser-disk player. Price depends on features, but expect to pay around \$1,000 for an auto-reverse model that plays both sides of a disk automatically. The Chinese offer a better bet



**HOME ENTERTAINMENT**



VCR—roughly 400 vs. es of horizontal reso- as well as CD-quality The downside is that deo stores rent laser they're expensive to and they don't allow ng. Also, the 12-in. disk is likely to be l late next year by a deo CD with an even picture.

third choice of source l is the digital satel- tem currently offered and Sony for about ot including installa- he high-quality digital is received by an 18- that is less obtrusive typical outdoor TV an Direct-broadcast satel- tems are also available Primestar. Its dish is but Primestar will e gear, rolling the cost monthly bill comparable e TV rates. Competing s are due from Al- and Echosphere next

**AND MIRRORS.** While n get by with a 27-in. oving up to a larger size is worth it. Di- w TVs use the tradi- RT display and top out n., the one exception a 40-in. model from shi. Of course, the big- e screen, the greater t: An RCA 32-in. model, 2750AT, lists for \$1,649, RCA's 35-in. G35851LA r \$2,499.

een sizes over 40 in. exclusively on projec- vs—you just can't a glass tube any big- ojection TVs use sep- color tubes and a va- f mirrors to enlarge cture. While projec- TVs are physically than direct-view TVs, is not as big an is- s you might think. new projection TVs re the same front-to- s direct-view models, y don't eat up addi- floor space. Toshiba's \$4,495 TP61E90 is

only 27 in. deep. Projection TVs also lend themselves to discreet in-wall installations. Of course, some are practically walls themselves, the biggest being an 80-in., \$8,000 monster from RCA.

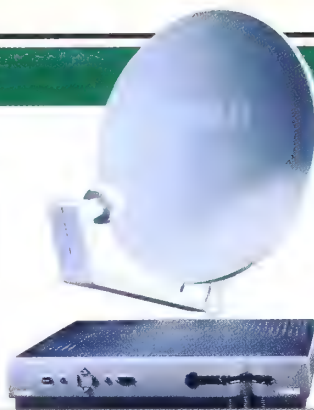
Historically, direct-view TVs have delivered a better picture than projection TVs, although the gap between the two is closing quickly. Still, brightness levels, resolution, and off-axis viewing tend to be better on direct-view models.

Perhaps the most complicated bit of business is the sound system. To duplicate the movie theater experience, you must be surrounded by speakers. The key ingredient is a circuit called Dolby Pro Logic, which directs the sound to the appropriate speaker. When you hear that helicopter coming in from behind you, that's Dolby Pro Logic at work.

Dolby can be incorporated into a TV or as part of a stand-alone audio receiver. If a TV includes Dolby Pro Logic circuitry, it generally means there are built-in amplifiers and speakers. The TV will also have some provision for connecting rear speakers. While convenient, the built-in arrangement usually comes at the cost of amplifier power and speaker performance. More pow-



**FIGURE:** A 35-in. direct-view screen



**ON THE BEAM:** RCA's dish is just 18 in. in diameter

onscreen dialogue. Otherwise, the spoken word can be overwhelmed by competing sounds or may appear to be coming from somewhere other than the actor's mouth. Sometimes, you may be able to use a built-in TV speaker as the center-channel speaker.

Behind you are a pair of rear speakers. These need not be expensive, as they will only be called on to reproduce sound at the lower portions of the audio spectrum. While five speakers will get you started, you may want to consider a sixth in a supporting role. A subwoofer, which reproduces low bass frequencies, will put thunder into the system.

**SAY "WHEN."** Where once you had to cobble together elements from a variety of brands, some companies now offer all the needed extras in one neat package. 3M markets its STV Digital 6 system that includes a Dolby Pro Logic processor with subwoofer and five speakers for a list price of \$599. If Dolby Pro Logic is built into your TV or audio receiver, you may want to opt for Kenwood's KSS-500 package. The list price of \$699 gets you five speakers and a subwoofer.

While Dolby Pro Logic is the dominant surround-sound technology, other types exist. RCA and Sony TVs employ an SRS circuit designed to

produce a surround effect with non-Dolby encoded video material. At the higher end, THX and AC-3 enhance the surround sensation but call for even more speakers. It's a truism in audio that incremental increases in performance cost a great deal. The same applies to home theater in general. It's up to you to say when enough is enough. *Frank Vizard*

## Casting Call

### SOURCE

**BASIC VIDEO** A hi-fi videocassette recorder with left- and right-channel audio outputs (\$250-\$600)

**THE STEP-UP** Laser-disk players offer better picture and sound than videotape (\$400 for auto-reverse model)

**THE ULTIMATE** Satellite TV's digital signal, featuring the best picture and sound available (monthly bill is comparable to cable-TV rates)

### SCREEN

**BARE MINIMUM** A 27-in. (diagonal) TV (\$400-\$900)

**THE MIDDLE GROUND** Big-screen, direct-view TV, primarily 32-in. and 35-in. feature-laden models (\$1,200-\$2,700)

**THE WOW-YOUR-FRIENDS SETUP** Projection-screen TV, ranging from 45 in. to 80 in. (\$2,400-\$8,000)

### SOUND

**MUST-HAVE** The Dolby Pro Logic circuit, which directs sound to the appropriate speaker

**STARTING FIVE** Three speakers up front and two in the rear, the basic surround-sound configuration (\$600-\$700 including Dolby Pro Logic)

**RAISE THE ROOF** A subwoofer to reproduce those deep bass frequencies (\$200-\$1,000)

DATA BUSINESS WEEK

er—whose purpose is better fidelity at lower volume levels—and improved sound reproduction generally require separate components.

You'll need five speakers for a superior system—three up front and two in the rear. In addition to the standard left- and right-channel speakers up front, you'll be well-served by a center channel speaker that anchors the





**MOVE OVER, CDs: LP**  
sales rose 58% in 1994

All this renewed interest in records is spawning a massive reissuing of the classics on LPS, both jazz and classical, from the late 1940s on and rock and pop from the late 1950s on. Even hot new recordings from best-selling artists are being released on vinyl: Recent ones include Bob Dylan's *MTV Unplugged* session, Pearl Jam's *Vitalogy* (actually appearing two weeks earlier than the CD), and Michael Jackson's *HIStory*. "We had just stopped doing LPS, period," says Epic Records President Richard Grifiths. "Then we figured out for certain artists there is a market out there."

Sure, the numbers are small. Only 70,000 *Vitalogy* LPS were shipped compared with 5 million CDs. But according to the Recording Industry Assn., unit sales of vinyl LPS were up 58% in 1994—after a decade of steadily declining sales dating back to the introduction of the CD in 1982. "The industry declared the LP was dead before it was," says Michael Fremer, a longtime audio writer who is editor of *The Tracking Angle*, a new magazine devoted to vinyl. "People have records. They have turntables."

During the digital decade, it was writers such as Fremer and artists such as Neil Young who continued to rail against CD sound, which they found too clinical and harsh. Meanwhile, a small group of independent record produc-

ers, artists, and music dealers kept analog alive by buying up record catalogs in Europe and Asia, where LPS continue to be made, and securing rights to reissue the classics of such artistically critical labels as Blue Note in jazz and RCA in classical. "The stuff sells very well because these are things that have been out of print for a long time," says Brian Dorn, manager of the Record Company in Princeton, N.J.

Stores such as Dorn's are treasure troves of old and new. He has 100,000 mostly used LPS, selling prices as low as \$4 with many recordings aging about \$4. New LPS from \$9 to \$10, considerably below today's average CD price of \$12 to \$13.

**WATER MUSIC.** Then there are mail-order houses such as Acoustic Sounds (800-355-3553), whose 300-page catalog is filled with LPS from artists as diverse as British folk group Pentatonix (\$25) to George Szell and the London Symphony Orchestra performing Handel's *Water Music* (a limited-edition reissue of the original recording on specialty label sells for \$35). "A lot of people sold their collections, and they call and want their stuff back," says Acoustic Sounds owner Chad Kisner. Vinyl devotees such as Kisner even report seeing scouring garage sales and flea markets, where old records can sometimes be found in abundance.

So, whether your record collection runs more to Mario Lanza or Mariah Carey, it may be time to crank up that old turntable and get those aging records out of the attic. As long as they have been stored in a dry place, they should be playable. And if you want to start fresh, consider selling the new, high-quality turntables that have come to market as part of the vinyl renaissance. Just think, in every day you can be hip and nostalgic at the same time.

Tim

## GOOD GOLLY MISS MOLLY—LPs ARE BACK

In the music world, it seems that everything old is new again. Led Zeppelin is big. So is Elton John. Even Tom Jones has recovered his stardom. But the retro trend goes beyond the musicians. A small but growing number of music lovers are rediscovering the joys of the long-playing record—enough to prompt the big labels to get back into the business of pressing vinyl.

Long since given up for dead by the major recording companies that turned the 1980s into the digital era, the old-fashioned 12-in. black disk is being brought back to life—at prices about 25% lower than today's standard compact disks. It's not just the aging Woodstock generation that's dusting off its Joni Mitchell albums: Generation

X-ers are embracing vinyl as contemporary bands such as Pearl Jam insist on also presenting their newest tunes in the analog format.

There are many audiophiles who maintain that LPS sound better than CDs, offering warmer tones that more naturally mimic the original recording ambience. That's debatable—and certainly depends a lot on the quality of the playback system. But who can argue that liner notes are much easier to read or that covers are more enticing on records than compact disks?

**HOME ENTERTAINMENT**

Many audiophiles maintain that LPs offer warmer tones than CDs



# THE FAMILY ALBUM GOES MULTIMEDIA

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**READ.** At the  
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e can keep a written  
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semblage of pictures,  
s, or sounds. Family

members can use passwords  
to hide the books in a wall  
safe. Those who want to  
share stories can print them  
out or dispatch them via  
diskettes to relatives. An  
Echo Lake viewer is copied  
onto the floppy, so recipients

need not own the  
program.

Those who delve  
further into the family tree  
will appreciate one of the nu-  
merous genealogy programs  
on the market. Among the  
best is Family Tree Maker  
from Banner Blue Software.  
The \$60 CD-ROM holds the  
names of 100 million deceased  
people. There are no actual  
records, just a listing of  
where to go to find better  
information.

Family Tree Maker lets

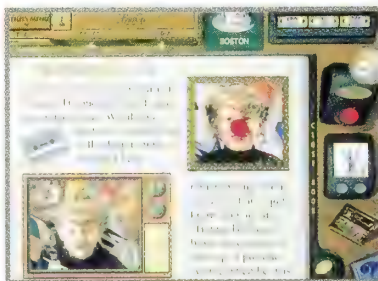
be transferred easily to other  
programs using the format.  
As with Echo Lake, you can  
import images and sounds.

To accomplish that, though,  
you need special equipment.  
Today's multimedia comput-  
ers are equipped with sound  
cards that let you plug in a  
microphone and record. With  
a \$330 video-capture-board,  
such as VideoBlaster  
SE100 from Creative  
Labs, users can import  
video clips that may be  
edited and played back  
off the hard disk.

**SCANNERS.** Folks who  
are dripping in cash can  
whisk photographs into  
their computer via a  
digital camera from the  
likes of Logitech and East-  
man Kodak. The cameras  
store images in computer files  
rather than on film. But at a  
list price of about \$1,000, dig-  
ital cameras are best used for  
business purposes. A cheaper  
and better bet is a scanner.

into a Windows word proces-  
sor or other programs.

Play Inc. recently intro-  
duced a nifty \$200 device  
called Snappy. The size of a  
cigarette box, it plugs into  
the parallel port and connects  
to a camcorder, VCR, or tele-  
vision. When you see a pic-  
ture you want to grab, click  
"Snap," and Snappy freezes



**KEEPSAKES:** Text, video,  
and sound from Echo Lake

the image. Snappy comes  
with morphing and paint soft-  
ware that lets you manipu-  
late images.

But you don't need sepa-  
rate gear to get photos into  
your PC. Seattle Film Works  
(800 445-3348) and Konica  
Quality Photo (800 669-1070)  
will transfer film onto  
diskettes. Both charge about  
\$4 on top of the regular pro-  
cessing costs for a 24-print  
roll, or \$6 for 36 images.

The disks include pro-  
grams that let you  
resize and crop pic-  
tures. Kodak has  
built a free soft-  
ware utility into  
Photo CD disks  
that also lets consumers re-  
cast images. Processing cost:  
about \$1 per picture.

Even for memories you  
don't intend to store on com-  
puter, a PC can come in  
handy. Gold Disk's Video-  
Director Home software lets  
users edit videotapes. The \$50  
program comes with a cable  
that connects a camcorder,  
VCR, and PC. You mark the  
start and end of sequences  
and drag and drop the scenes  
into any order you desire.  
Scenes are then copied from  
camcorder to VCR. Alas,  
you're on your own in get-  
ting others to watch the  
results.

Edward Baig



you keep tabs on  
marriages, educa-  
tional backgrounds, births,  
deaths, and other data on  
your relatives. One user  
traced his family's history  
with Lou Gehrig's disease.  
The software is GEDCOM (ge-  
nealogical data communica-  
tions)-compliant, so files can

EasyPhoto Reader which  
plugs into the printer port  
on your computer. Color  
photos are scanned into a  
motorized feeder, then  
EasyPhoto software organizes  
thumbnail copies of your pic-  
tures into a gallery. You can  
resize, rotate, or crop the pic-  
tures and add titles. Photos  
can be dragged and dropped

Storm Soft-  
ware has a  
simple \$269  
product called



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of companies large  
and small to join this  
concerned group of  
business leaders.  
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for business.  
Look beyond our  
disabilities and  
all America  
gains."

Jim Brady, Vice Chairman  
National Organization  
on Disability

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with disabilities.  
Through their individual  
membership contributions,  
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# Business Week Index

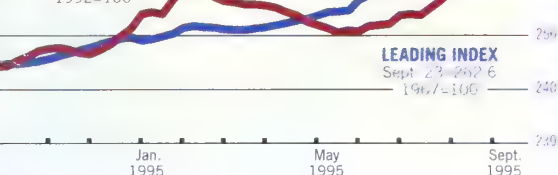
## PRODUCTION AND LEADING INDEXES

Change from last week: 0.6%  
Change from last year: 8.0%

Change from last week: 1.1%  
Change from last year: 7.1%

### PRODUCTION INDEX

Sept. 23=125.4  
1992=100



are 4-week moving averages

Production index was down during the week ended Sept. 23. Before the four-week moving average, the index dropped to 123.3, from the previous week. The recent weakness is because of the declines in adjusted output of electric power, coal, and trucks.

Leading index was virtually unchanged in the latest week. The unadjusted index rose to 261.9, from 263.8. Falling materials prices are pointing to softness ahead.

Production index copyright 1995 by The McGraw-Hill Companies BW leading index copyright 1995 by CIBC

## FINANCIAL INDICATORS

|                                                 | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|-------------------------------------------------|-------------|------------|--------------|
| STOCK PRICES (9/30) S&P 500                     | 582.91      | 583.69     | 26.0         |
| GOVERNMENT BOND YIELD, Aaa (9/30)               | 7.33%       | 7.31%      | -13.6        |
| COMMODITY MATERIALS PRICES (9/30)               | 112.2       | 112.8      | NA*          |
| INSURANCE CLAIMS FAILURES (9/22)                | 313         | 307        | -1.3         |
| HOUSING STARTS (9/20) billions                  | \$497.0     | \$499.3    | 11.7         |
| CREDIT SUPPLY, M2 (9/18) billions               | \$3,717.8   | \$3,713.2r | 4.0          |
| UNEMPLOYMENT CLAIMS, UNEMPLOYMENT (9/16) thous. | 366         | 364        | 14.0         |

\*Center for International Business Cycle Research (CIBC), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures companies), Federal Reserve, Labor Dept. CIBC seasonally adjusts data on failures and real estate loans. \*Historical data available from CIBC

## BEST RATES

|                                           | LATEST WEEK | WEEK AGO | YEAR AGO |
|-------------------------------------------|-------------|----------|----------|
| MONEY FUNDS (10/3)                        | 5.75%       | 5.73%    | 5.07%    |
| COMMERCIAL PAPER (10/3) 3-month           | 5.81        | 5.76     | 5.49     |
| SAVING DEPOSITS OF DEPOSIT (10/4) 3-month | 5.78        | 5.78     | 5.51     |
| FIXED RATE MORTGAGE (9/29) 30-year        | 7.89        | 7.82     | 8.91     |
| ADJUSTABLE MORTGAGE (9/29) one-year       | 5.79        | 5.80     | 5.69     |
| 10/4)                                     | 8.75        | 8.75     | 7.75     |

Federal Reserve, HSH Associates, Reuters Holdings PLC

## PRODUCTION INDICATORS

|                                                 | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|-------------------------------------------------|-------------|-----------|--------------|
| STEEL (9/30) thous. of net tons                 | 1,934       | 1,955#    | 1.4          |
| AUTOS (9/30) units                              | 139,170     | 132,228r# | 16.4         |
| TRUCKS (9/30) units                             | 125,337     | 117,406r# | 10.5         |
| ELECTRIC POWER (9/30) millions of kilowatt-hrs. | 58,979      | 61,631#   | 1.8          |
| CRUDE-OIL REFINING (9/30) thous. of bbl./day    | 14,280      | 14,298#   | 1.5          |
| COAL (9/23) thous. of net tons                  | 20,650#     | 20,842    | 3.2          |
| PAPERBOARD (9/23) thous. of tons                | 858.9       | 867.6r    | -4.6         |
| PAPER (9/23) thous. of tons                     | 843.0       | 835.0r    | 1.7          |
| LUMBER (9/23) millions of ft.                   | 477.7#      | 475.1     | -3.9         |
| RAIL FREIGHT (9/23) billions of ton-miles       | 25.3#       | 25.6      | 5.0          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA<sup>1</sup>, SFPA<sup>2</sup>, Association of American Railroads

## PRICES

|                                                      | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|------------------------------------------------------|-------------|----------|--------------|
| GOLD (10/4) \$/troy oz.                              | 382.500     | 383.750  | -2.9         |
| STEEL SCRAP (10/3) #1 heavy, \$/ton                  | 143.50      | 143.50   | 7.5          |
| COPPER (9/29) \$/lb.                                 | 136.7       | 135.6    | 8.5          |
| ALUMINUM (9/29) \$/lb.                               | 82.0        | 82.0     | 3.8          |
| COTTON (9/29) strict low middling 1-1/16 in., \$/lb. | 88.65       | 92.53    | 28.8         |
| OIL (10/3) \$/bbl.                                   | 17.57       | 17.33    | -0.7         |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                                  | LATEST WEEK | WEEK AGO | YEAR AGO |
|----------------------------------|-------------|----------|----------|
| JAPANESE YEN (10/4)              | 101.17      | 100.15   | 99.94    |
| GERMAN MARK (10/4)               | 1.44        | 1.43     | 1.54     |
| BRITISH POUND (10/4)             | 1.58        | 1.57     | 1.59     |
| FRENCH FRANC (10/4)              | 4.96        | 4.92     | 5.27     |
| ITALIAN LIRA (10/4)              | 1613.3      | 1605.5   | 1570.4   |
| CANADIAN DOLLAR (10/4)           | 1.33        | 1.35     | 1.35     |
| MEXICAN PESO (10/4) <sup>3</sup> | 6.535       | 6.395    | 3.417    |

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### COMMODITY PRICE INDEX

Oct. 12, 8:30 a.m. ▶ Producer finished goods likely rose a small September, according to the median of economists surveyed by MMS. One of the McGraw-Hill Cos. it would be the first increase in price since May. August producer prices rose 0.1%. And over the past year, the PPI rose only 1.2%. The forecast expects producer prices, which exclude energy, also rose 0.2% last month after rising 0.1% in August. Pro-inflation may have been even weaker in September, though. The National Association of Purchasing Management's index of prices paid by its members for supplies and

materials fell to its lowest level in nearly three years in September.

### RETAIL SALES

Friday, Oct. 13, 8:30 a.m. ▶ Retail sales probably increased 0.4% in September, forecasts the MMS survey. That's suggested by the rise in weekly sales at department and chain stores reported by the Johnson Redbook Service, a unit of brokerage firm Lynch, Jones & Ryan Inc. Excluding cars, store receipts likely advanced 0.5% last month. In August, strong car sales led to a 0.6% surge in total retail buying. Nonauto sales, however, were flat. While furniture purchases were up sharply, a poor back-to-school buying season was blamed for falling

receipts at clothing and department stores. And falling gasoline prices held down gas station revenues.

### CONSUMER PRICE INDEX

Friday, Oct. 13, 8:30 a.m. ▶ The MMS forecast calls for a 0.2% rise in September consumer prices. Prices in August increased just 0.1% as falling energy prices offset price hikes in meats and tobacco products. Excluding food and energy, core consumer prices likely increased by 0.2% in September, the same increase posted in each of the previous four months. After showing signs of growing above 3% in early 1995, consumer inflation has slipped back down to a 2.6% yearly pace.



# This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

**ONLINE**  
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## Sunday

The Bankers Trust tapes—and Business Week's First Amendment fight: Talk with McGraw-Hill lawyer Ken Vittor and BW's Sarah Bartlett about this landmark battle.

**Oct. 8**

**9 p.m. EDT in the Globe**

## Wednesday

Installing Windows 95—dream or nightmare? Share your experiences with an expert guide, Steve Wildstrom of BW's Technology & You column.

**Oct. 11**

**10 p.m. EDT in the Odeon**

## Thursday

Perot in 1996? Discuss the prospects for a third-party candidate in the next election (Colin Powell, anyone?) with BW's Washington bureau chief, Lee Walczak.

**Oct. 12**

**9 p.m. EDT in the Odeon**

*Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.*

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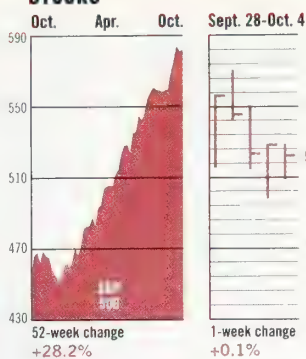
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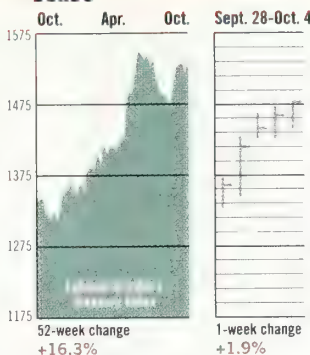
# Investment Figures of the Week

**MARKET**  
Economic reports kept in-  
vigor. Factory orders and  
shipped up in August,  
has boosted consu-  
g. But personal incomes  
same, and manufacturers  
fall for the fourth time  
in September. Bond  
trading that weaker-than-  
growth would lead the Fed-  
to lower interest rates  
ear, bid up the price on  
suries. That sent the  
from 6.58% to 6.43%.  
a down week as tech  
up some ground.

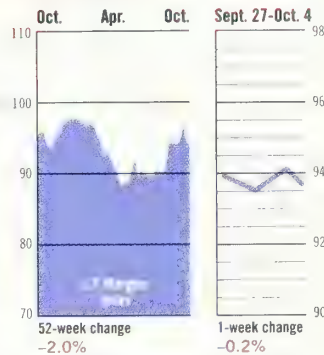
## STOCKS



## BONDS



## THE DOLLAR



## ANALYSIS

|                                         | Latest  | % change                  |         |
|-----------------------------------------|---------|---------------------------|---------|
|                                         |         | Week                      | 52-week |
| <b>INDUSTRIALS</b>                      | 4740.7  | -0.5                      | 25.2    |
| <b>COMPANIES (S&amp;P MidCap Index)</b> | 209.7   | -1.7                      | 22.8    |
| <b>COMPANIES (Russell 2000)</b>         | 300.8   | -1.6                      | 20.6    |
| <b>COMPANIES (Russell 3000)</b>         | 332.9   | -0.3                      | 27.5    |
|                                         | Latest  | % change (local currency) |         |
|                                         |         | Week                      | 52-week |
| <b>FINANCIAL TIMES 100</b>              | 3544.1  | 1.7                       | 19.9    |
| <b>FTSE 100 INDEX</b>                   | 18145.1 | -0.6                      | -8.1    |
| <b>EURO COMPOSITE</b>                   | 4492.6  | -0.2                      | 5.6     |

## FUNDAMENTALS

|                                         | Latest | Week ago | Year ago |
|-----------------------------------------|--------|----------|----------|
| <b>90-DAY TREASURY BILL YIELD</b>       | 5.45%  | 5.41%    | 5.07%    |
| <b>30-YEAR TREASURY BOND YIELD</b>      | 6.43%  | 6.58%    | 7.95%    |
| <b>S&amp;P 500 DIVIDEND YIELD</b>       | 2.34%  | 2.34%    | 2.80%    |
| <b>S&amp;P 500 PRICE/EARNINGS RATIO</b> | 16.8   | 16.8     | 17.9     |

## TECHNICAL INDICATORS

|                                                  | Latest | Week ago | Reading  |
|--------------------------------------------------|--------|----------|----------|
| <b>S&amp;P 500 200-day moving average</b>        | 521.6  | 518.4    | Positive |
| <b>Stocks above 200-day moving average</b>       | 72.0%  | 72.0%    | Negative |
| <b>Speculative sentiment: Put/call ratio</b>     | 0.66   | 0.64     | Neutral  |
| <b>Insider sentiment: Vickers sell/buy ratio</b> | 2.72   | 2.69     | Negative |

BLOOMBERG FINANCIAL MARKETS

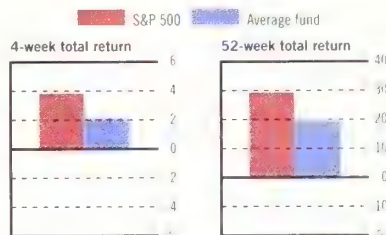
## GROUPS

|                 | % change |          |                                   | % change |          |        |
|-----------------|----------|----------|-----------------------------------|----------|----------|--------|
|                 | 1-month  | 12-month |                                   | 1-month  | 12-month | Price  |
| <b>LEADERS</b>  |          |          | <b>Strongest stock in group</b>   |          |          |        |
|                 | 16.4     | -15.1    | <b>UNITED HEALTHCARE</b>          | 17.6     | -7.3     | 49 1/4 |
|                 | 15.5     | 81.3     | <b>TEKTRONIX</b>                  | 28.0     | 54.1     | 58 1/8 |
|                 | 14.9     | 41.3     | <b>NIKE</b>                       | 24.3     | 94.9     | 115    |
|                 | 14.1     | 55.0     | <b>SCHERING-PLOUGH</b>            | 15.8     | 47.6     | 53 1/8 |
|                 | 11.3     | 49.9     | <b>PEPSICO</b>                    | 14.3     | 54.7     | 52     |
| <b>LAGGARDS</b> |          |          | <b>Weakest stock in group</b>     |          |          |        |
|                 | -12.8    | 3.1      | <b>CROWN CORK &amp; SEAL</b>      | -12.9    | 0.7      | 39     |
|                 | -11.1    | 6.9      | <b>CATERPILLAR</b>                | -19.0    | 1.8      | 55 1/4 |
|                 | -9.0     | -30.2    | <b>INLAND STEEL INDUSTRIES</b>    | -17.5    | -42.4    | 22 1/8 |
|                 | -8.8     | 1.6      | <b>ROWAN</b>                      | -11.8    | 3.5      | 7 1/4  |
|                 | -8.2     | -2.8     | <b>BROWNING-FERRIS INDUSTRIES</b> | -9.7     | -5.8     | 30 1/8 |

MORNINGSTAR INC.

## FUNDS

|                                             | %     | <b>LAGGARDS</b>               | % |
|---------------------------------------------|-------|-------------------------------|---|
| <b>Four-week total return</b>               |       | <b>Four-week total return</b> |   |
| <b>WRIGHT EQUIFUND-MEXICO</b>               | -5.3  |                               |   |
| <b>ARCH EMERGING GROWTH INSTITUTIONAL</b>   | -5.1  |                               |   |
| <b>FIDELITY SELECT INDUSTRIAL EQUIPMENT</b> | -5.0  |                               |   |
| <b>52-week total return</b>                 |       | <b>52-week total return</b>   |   |
| <b>WRIGHT EQUIFUND-MEXICO</b>               | -51.9 |                               |   |
| <b>BT INVESTMENT LATIN AMERICAN EQUITY</b>  | -40.7 |                               |   |
| <b>HERCULES LATIN AMERICAN VALUE</b>        | -38.8 |                               |   |



## PORTFOLIOS

Units represent the  
value of \$10,000  
one year ago  
portfolio  
Returns indicate  
total returns



**U.S. stocks**  
**\$13,191**  
+0.16%



**Treasury bonds**  
**\$12,707**  
+1.69%



**Foreign stocks**  
**\$10,973**  
+0.70%



**Money market fund**  
**\$10,545**  
+0.12%



**Gold**  
**\$9,659**  
-0.42%

GRUBB GROW HILL

This page is as of market close Wednesday, Oct. 4, 1995, unless otherwise indicated. Mutual fund returns are as of Sept. 29. Relative portfolios are valued as of Oct. 3. A more detailed explanation of this page is available on request. r=revised

of market close Oct. 3. Mutual fund returns are as of Sept. 29. Relative portfolios are valued as of Oct. 3. A more detailed explanation of this page is available on request. r=revised



## FURTHER THOUGHTS ON FREEDOM OF THE PRESS

Now you can read it for yourselves. BUSINESS WEEK's cover story, "The Bankers Trust tapes," banned from publication by a U.S. District Court for more than three weeks, is finally free to be read by the public. Also freed from the veil of secrecy are the sealed documents at the heart of a \$195 million lawsuit by Procter & Gamble Co. against Bankers Trust Co. The public can at last see the data and decide for itself if P&G's charges that Bankers Trust engaged in a pervasive pattern of fraud are true.

But the cost has been high. The freedom of the press to generate the kind of information necessary for the efficient operation of this nation's political and economic system appears to have been seriously eroded in the legal process of getting the story out. First, a judge of the U.S. District Court for the Southern District of Ohio banned publication of an article with no hearing on the facts. Supreme Court Justice John Paul Stevens ruled that this judge was in violation of the Federal Rules of Civil Procedure, but he nevertheless continued for three weeks to ban the story on Bankers Trust.

The second troubling development came when Stevens contended that "the manner in which BUSINESS WEEK came into possession of the information it seeks to publish may have a bearing on its right to do so." In all previous cases, the method of acquiring the information was not held to be relevant to whether or not it could be published. The Pentagon Papers, after all, were stolen. BUSINESS WEEK lawfully obtained its documents, but if it hadn't, whoever unlawfully obtained them could have been punished. The goal should be to punish the thief, not bar publication. Censorship cannot be the solution to a crime of theft.

Third, the final opinion of the U.S. District Court judge prohibits newspapers, magazines, or any electronic media from even asking for a document that is stamped by a court "sealed," "confidential," or "secret." It is a bizarre interpretation of *Seattle Times v. Rhinehart* (1984), in which the Supreme Court held that a party to a protective court order

covering pretrial information developed in discovery could divulge the information. BUSINESS WEEK was never a party to the P&G lawsuit against Bankers Trust, but the judge declared that it should be prohibited from even asking for documents under seal.

This is a wildly dangerous opinion if upheld. There is nothing in current law saying that people who are not party to an agreement to seal court documents are forbidden from asking to see them. This opinion makes the protection to ensure court confidentiality more important than the First Amendment. Any court official with a rubber stamp could block the free flow of information in this country. This is not acceptable. The media have the right to ask for information. Sources can say no anytime. Does America really want to move toward a British system of press restrictions, in which, for example, a Thalidomide case was litigated for years in the courts while the media was barred from reporting on it as hundreds of women continued to take the drug? We think not.

Finally, the bedrock principle that a journalist is entitled to protect the identity of a source, we were reminded, is not universally applied. In trying to lift the ban on publishing the Bankers Trust tapes, BUSINESS WEEK reporters came up against the reality that shield laws protecting the confidentiality of sources vary from state to state and judge to judge. In Ohio, the shield law covers newspapers, but not magazines. There is no federal shield law covering the entire country.

Much of this damage to freedom of speech can be repaired in the weeks ahead as BUSINESS WEEK appeals the opinion of the U.S. District Court. The media must be free to report on judicial proceedings and on government operations in general. If there is legitimate need for confidentiality, it is up to the parties to maintain it. But once information is obtained by the press, it must be able to disseminate it to the public. The Supreme Court has held over many years, prior restraint is an unconstitutional form of censorship. Period.

## WHY GIVE THE AIRWAVES AWAY?

Make them pay for spectrum. Broadcasters are about to succeed in getting the government to hand over nearly \$40 billion worth of precious airwave space. At a time when Congress is struggling hard to balance the budget, it is ludicrous to offer this freebie.

What's going on? In 1992, when the Japanese appeared to be winning the battle for high-definition TV, the government gave a huge block of spectrum to U.S. broadcasters to help them compete. Three years later, HDTV is a commercial dud, but broadcasters still want the spectrum. With new digital technology, they can send lots of channels into the home.

Since 1994, the Federal Communications Commission has

been auctioning off the airwaves. To date, it has put \$800 million into the federal coffers. The spectrum handed out is worth many times that, but the broadcasters don't want to pay for it. They prefer the old days, when the government simply gave out spectrum, free of charge, for everything from garage door openers.

Senate Commerce Committee Chairman Larry Pressler (R-S.D.) recently floated a plan that would have auctioned off frequencies in the top 25 markets, but lobbyists forced him to back off. We hope Pressler rediscovers his political courage and does the right thing. Sell the spectrum to the highest bidder, and use the money to pay down the government's

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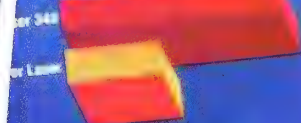
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SS WEEK  
October 23

# BusinessWeek

ER 23, 1995

A PUBLICATION OF THE MCGRAW-HILL COMPANIES



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# BLIND AMBITION

ausch & Lomb CEO Daniel Gill pushed hard  
or profits. To meet his goals, some managers  
played fast and loose with accounting principles  
and ethics. Here's how the relentless pursuit of  
results caused one  
company's culture to  
spin out of control.

BY MARK MAREMONT

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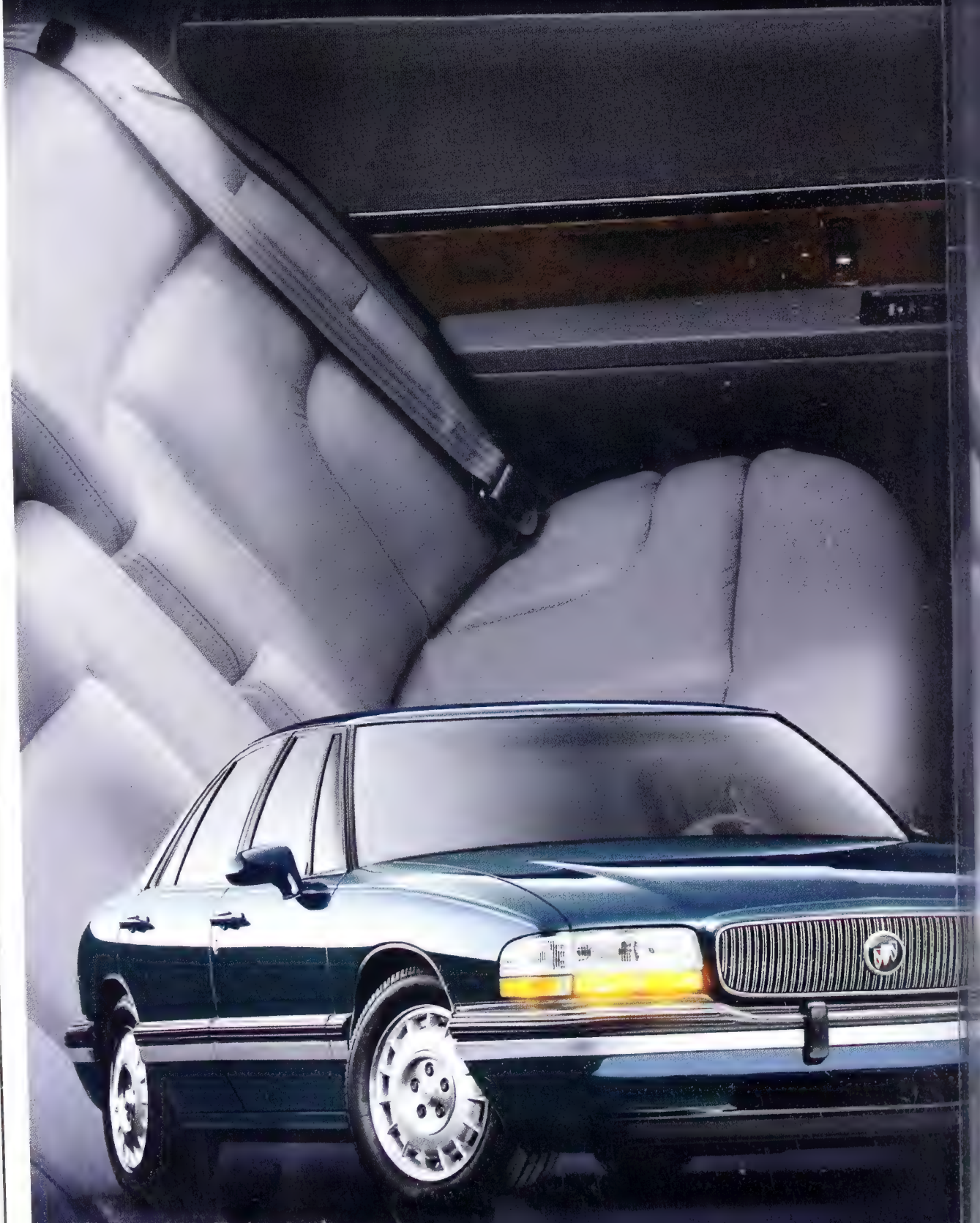
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# BusinessWeek

OCTOBER 23, 1995



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# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

## MOTOR CITY

### BREAKING THE MOLD AT GM

IS GENERAL MOTORS taking a blowtorch to its notorious "frozen middle"? Its infamously change-resistant ranks are about to get a shakeup when GM names newly created marketing and product-development honchos Oct. 19 and 20. As these new managers gain more power, company insiders predict some of their hide-bound bosses—at least 500—will take buyouts and retire.

Some 16 to 18 new development czars, or vehicle line executives, will each oversee



DRAWING BOARD: A GM designer

engineering, styling, and manufacturing for a new family of cars or trucks. The jobs actually have tenure—8 or 10 years. Among the fast-track execs rumored to be tapped:

**TALK SHOW** "It's not clear to me what is going on in the Congress."

—President Bill Clinton, responding to congressional Republican complaints that he's not negotiating seriously on the federal budget

Michael Grimaldi, head of planning for North American operations; James Taylor, head of truck purchasing; Larry Lyons, chief engineer for luxury cars; Gary White, Olds chief engineer; David Hill, Corvette chief engineer; and Freek Schaafsma, mini-van program manager.

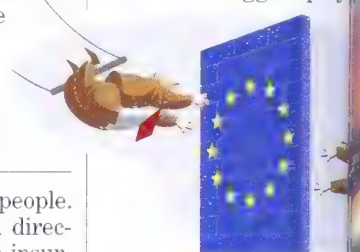
Aspirants for the 34 marketing posts, called brand managers, must undergo grueling, all-day sessions doing a marketing plan for a hypothetical model. Another new twist: Each GM auto division, except Saturn, will hire one outsider as a brand manager. Most of those six are expected to have packaged-goods marketing credentials.

Keith Naughton and Kathleen Kerwin

## THE DEAL MILL

### THE EU GOES TRUSTBUSTING

KIMBERLY-CLARK AND Scott Paper have hit a snag in their merger plans. The European Union is launching an antitrust probe that could end up forcing the paper goods companies to sell a chunk of their assets in Europe, where combined sales exceed \$2 billion. In the U.S., the deal is under a Justice Dept. review, results expected by November. As the biggest play



Europe's merger wave, companies are getting hard by the EU's feisty competition authority. The EU is involved in about 25 of the antitrust cases this year.

In the Kimberly-Clark Scott Paper case, the Europeans fear a squeeze against local market leaders in Britain, where Kimberly-Clark's new giant would control some 25% to 30% of the toilet paper market. (It has one-third in the U.S.) The EU competition unit last year forced Procter & Gamble to divest certain European businesses before it could acquire V.P. Schick. Earlier this year, the commission started an inquiry into U.S. packaging giant Crown Cork & Seal's proposed acquisition of French metalbox manufacturer Metalbox of France, also keeping a close eye on America Online, Sprint, and AT&T as they take advantage of Europe's market opening in telecom. Linda E.

## LITIGATION NATION

### WHY OUTSIDE DIRECTORS HAVE NIGHTMARES

FOR CORPORATE DIRECTORS these days, getting slapped with a lawsuit is almost part of the job description. A new Louis Harris poll of 500 outside directors finds that more than 40% have been targets of a suit. Worse, they feel that the company-provided insurance coverage for suits falls short of the mark. Almost one-third of those polled have declined to serve on a board—or resigned from one—because of insurance worries.

How valid are these concerns? Well, taking just shareholder suits, a recent study by National Economic Research Associates says settlements rose from 103 in 1991 to 183 in 1994. Vinita Juneja, a NERA senior consultant, suspects the number may be down a bit this year, thanks

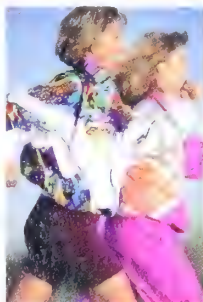
to talk of tort reform in Washington, but "that may be temporary." In addition to shareholder lawsuits (usually filed only after the stock takes a dive), the disgruntled sue for everything from wrongful firing to discrimina-

tion against disabled people.

Trouble is, so-called directors and officers (D&O) insurance may not cover every possible liability out there. Says Mark Rosen, vice-president at Executive Risk, the major D&O carrier that commissioned the Harris survey: "Some financial institutions, for instance, don't cover suits by regulators." □

### THE LIST WALK, DON'T RUN

For the one in six Americans who exercises frequently, fitness walking is most popular. Small wonder. Unlike resistance machines and



NOT A LEISURELY STROLL

aerobics, where you need costly equipment or club memberships, fitness walking is a budget operation. This is fast walking, not a leisurely sidewalk stroll—but less demanding than running.

### MOST POPULAR FITNESS ACTIVITIES

TOTAL EXERCISE PERSON DAYS PER YEAR\* IN MILLIONS

|                         |       |
|-------------------------|-------|
| FITNESS WALKING         | 4,034 |
| FREE WEIGHTS            | 2,779 |
| RUNNING/JOGGING         | 2,559 |
| STATIONARY BIKES        | 2,234 |
| FITNESS BICYCLING       | 1,483 |
| TREADMILLS              | 1,418 |
| RESISTANCE MACHINES     | 1,173 |
| FITNESS SWIMMING        | 1,010 |
| STAIR-CLIMBING MACHINES | 972   |
| LOW-IMPACT AEROBICS     | 724   |

\* Americans age 6 or older who participated at least once in year, multiplied by their average number of days of participation, 1994

DATA: AMERICAN SPORTS DATA INC.



OW TERRY HOOPER MADE THE WISE DECISION

TO DUMP HER STOCK IN THE MIDDLE OF A LAKE.



PRICE FALLING FAST  
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PAGENET

**8:21 A.M.**

*The lake makes for a well-deserved break. A page from her broker informs that the risky stock purchase opened at 7 7/8.*

**10:46 A.M.**

*Bad news. After sitting on her sunglasses, she sees that it dropped to 5 3/4.*

**12:27 P.M.**

*Sell quickly to avoid a total loss? No, she digs her feet into the soft sand and waits. It climbs back to 7.*

**2:42 P.M.**

*The fluctuating stock jumps and she sells before the bottom drops out. A relaxing day has turned a small profit financially, and a big one mentally.*

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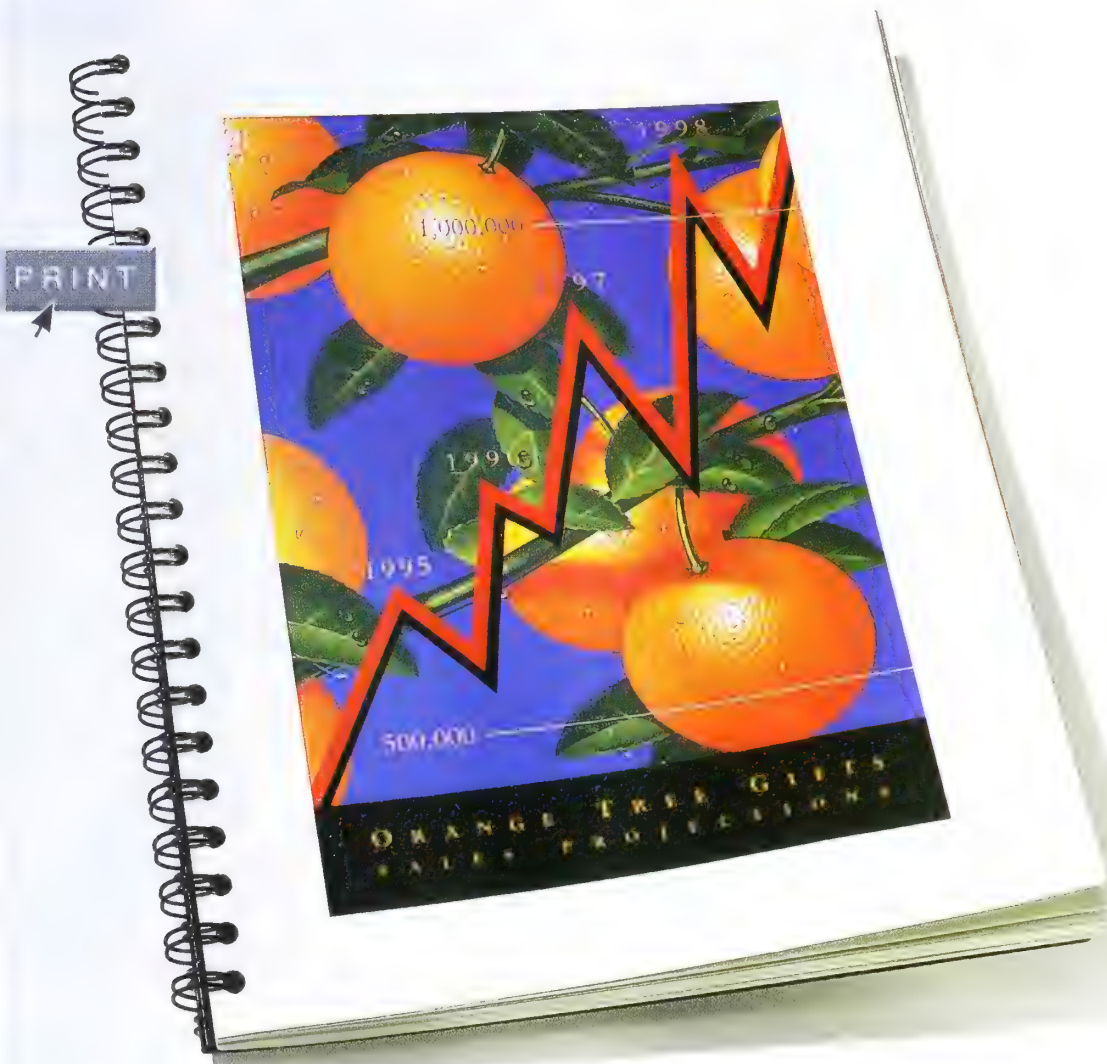
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## I-WAY PATROL

### A NUMBERS GAME FOR NET SURFERS

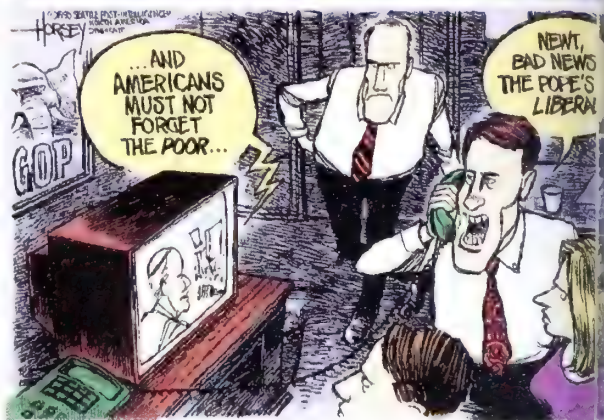
LOTTERY PLAYERS NOW CAN skip the convenience store and play on the Internet—from a World Wide Web site in Liechtenstein. The weekly drawings are run by the International Lottery in Liechtenstein Foundation, a not-for-profit organization chartered by the principality. InterLotto, as it's called, helps raise money for charities such as the Red Cross. Players pick 6 of 40 numbers from the home page

(<http://www.interlotto.li>), paying an entry fee of five Swiss francs (\$4.33) via MasterCard or EuroCard. Nobody drew the numbers to win the roughly \$1.3 million in the first drawing on Oct. 7.

Can hackers learn players' card numbers? InterLotto says players must use Netscape's Web Browser software, which InterLotto says is secure. Just in case players still aren't reassured, InterLotto also accepts credit card data via fax or post.

No one has started a Net lottery in the U.S., because regulators are unclear as to

**InterLotto**



## FUNNY BUSINESS

### IF A CON ANSWERS...

THE HOME OFFICE FOR THIS telecommuting scammer is—appropriately—the slammer. That's what Texas authorities say about Alan Todd May, a prisoner in Houston's Harris County Jail. He allegedly used the community phone in his cell block to raise money for five conventions that never occurred, bilking hundreds of unsuspecting exhibitors out of deposits they paid to reserve booths.



While serving time for writing bad checks and credit-card fraud, May charged

how to license and oversee one. In the Caribbean, there are Internet games of blackjack and roulette. InterLotto tells players to see if they can legally play. Some states, such as Florida, ban out-of-state gambling. *Paul Eng*

exhibitors from \$600 to \$2,000, police say. Over the past year, the victims sent their checks to his administrative assistant—who interviewed for the job in the jail visitors' room. Police say May booked space for such fictitious events as the Women's Business & Health Show and the Christian Family Expo. He even ran ads in newspapers, including *The Wall Street Journal* and *The Dallas Morning News*. Says Houston Police Sergeant J.B. Haney Jr.: "The guy's dangerous near a phone."

The assistant and an electronic paging service fostered the semblance of a respectable business. If noise from other inmates intruded on his calls, May would "just say he was on the road or at some convention," says Charlotte Mervin, catering sales manager for the Adam's Mark hotel in Denver. She said May reserved but never paid for convention space and services there.

May, who didn't respond to a request for comment, hasn't been formally charged while officials investigate. In the meantime, his jailhouse phone privileges have been revoked. *Kate Murphy*

## LEGAL-EASE

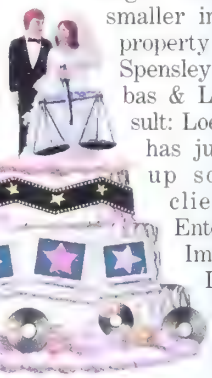
### WELCOME TO THE INTERACTIVE FIRM

THE CONVERGENCE OF technology and entertainment is driving corporate mergers and partnerships being copied by law. Experts in traditional entertainment and media law scrambling to add attorneys adept at intellectual property rights for CD-ROMs, games, interactive cable.

Look at Loeb & Loeb, a venerable Los Angeles entertainment firm. Recently merged with the smaller intellectual property specialist Spensley Hobas & Lubitz, the result: Loeb & Loeb has just signed up some clients. Entertainment Imaginative International Media and Interactive.

ner Philip Grosz says should boost 1995 profit to 15%.

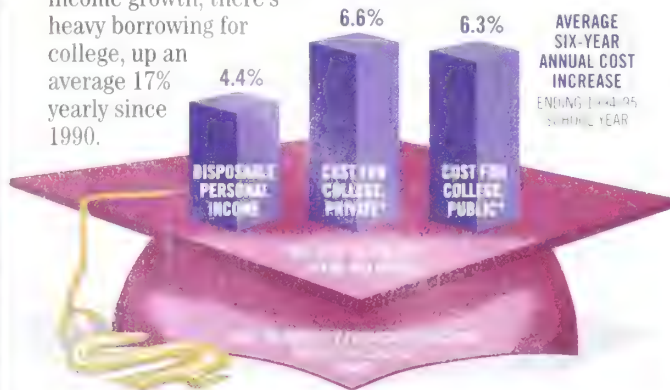
Fenwick & West is software rights. And Mann, Wolff, Bergmann & Silverman has sent Hollywood stars Selleck, Tracey Ullman. Their new joint venture attracted client Energyductions, which needs help as it digitizes such footage as sunsets.



## THE BIG PICTURE

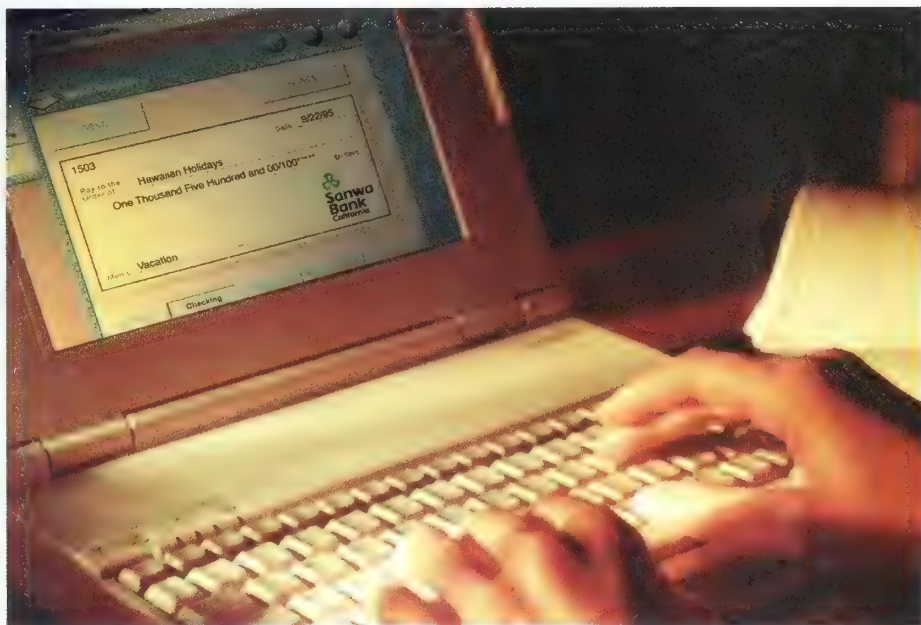
### FOUR YEARS OLDER AND DEEPER IN DEBT

A College Board survey says 1995-96 is the third straight year tuition costs have risen by 6%. Since the rise outpaces income growth, there's heavy borrowing for college, up an average 17% yearly since 1990.



**FOOTNOTES** Cash, as share of U.S. households' assets, 1990: **13.8%**; 1995: **10.7%**

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new signage, better ticketing, check-in and recheck.



our fast-growing network of worldwide  
ons, and many more improvements to come.  
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you will recognize a fresh spirit within China

pirit that is strong, committed, and constantly  
to be better, every day.

ows a determination to be not only Taiwan's

best airline, but one of the world's best.

And from now on, we carry the pink plum blossom  
with pride, from Taiwan to the world.

We blossom every day.

CHINA AIRLINES

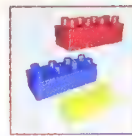




Joshua Denberg, Inventor of "Third Arm Carry-All" Patent



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# To Prevent Benefits Decay, Give Your Dental Plan An Annual Check-Up.



Without appropriate care, your dental plan could be eating away at your bottom line. To ensure you're not spending more to get less than you should, make certain that any dental plan you select includes these essentials:

**Comprehensive preventive care** with at least two dental exams and cleanings per year. Some plans don't include fluoride or sealants. Yours should. These treatments help prevent cavities, which brings down the cost of care.

**Flexibility in appointment scheduling.** Many insurers encourage their participating dentists to schedule "plan patients" as fill-in appointments. Your employee may have to take time off during the day to receive dental treatment or wait months to be seen. That's not only a problem for the patient, it costs you valuable employee time.

**Plans that allow patients to visit the dentists and specialists of their choice.** Research proves that patients won't go to dentists they don't trust. So you wind up paying the premium for unused benefits.

**Emergency, weekend and holiday care.** A plan that doesn't cover the unexpected is of no benefit to you or your employees. The emergency that isn't taken care of immediately can cost you dollars in downtime.

**Broad therapeutic coverage.** A plan that covers crowns and bridges, braces and dentures and even root canals may cost somewhat more, but will be more satisfactory to all plan users. Make sure that limitations on this kind of care are not unrealistically severe. You'll get fewer complaints even though employee co-payments are higher

for these services than for preventive care.

To make sure your dental plan provides acceptable protection for its beneficiaries, write, call or fax the California Dental Association for our "Consumer's Guide to Dental Insurance." It's designed to help you ensure that the dental plan you select provides the essentials of good oral health and runs on good business sense, too.



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## WHEN A JUDGE PLAYS EDITOR

The order by federal judge John Feikens, barring BUSINESS WEEK from running a legally obtained story, is clearly unconstitutional ("The story behind the Bankers Trust story," News: Analysis & Commentary, Oct. 2). As a retired journalism professor who lectured on prior restraint for many years, I completely support your position. Precedent from the Pentagon Papers decision of June 25, 1971, is clearly on your side.

It is vital that the public understand that imposing prior restraint on a publication goes beyond undermining just the rights of a magazine under the First Amendment. To the extent that the media are deprived of their rights, so are the rest of us. Even a whiff of totalitarianism can balloon into a stench.

Frank Grazian  
Professor Emeritus  
Rowan College of N.J.

By succumbing to court orders and failing to print a story using legally obtained information, BUSINESS WEEK has failed to uphold its duty to protect our First Amendment rights. Hiding behind an editorial statement that "BUSINESS WEEK, of course, is not above the law" hardly excuses this irresponsibility.

Our First Amendment rights are necessarily diminished when a major publication concedes that lower courts can arbitrarily forbid publication of a story obtained by legal means, even if only temporarily. The media is responsible first and foremost to the people and the protection of our right to free speech. Seek forgiveness, never permission, for upholding higher principles.

Emil Ronchi  
Unadilla, N.Y.

The First Amendment provides protection of free speech by the press, but it specifies no time frame in which this must occur. The two parties in litigation have a contract dispute that they wish to have resolved by the court. No criminal activity has been determined

## CORRECTIONS & CLARIFICATIONS

In "The Big Picture" (Up Front, Oct. 16, 1995), the percentages of companies offering certain benefits to employees after severance were misstated. The correct figures are, for health care, 65%; life insurance, 36%; pension credit, 17%; long-term disability, 14%.

"Team Disney's unknown stars" (People, Oct. 2) should have said that Stephen F. Bollenbach received his M.S. in management from California State University at Northridge.

to exist, so why is it not fair for either of the litigating parties to want a clamp placed on records of the case and for that request to be respected?

Evidently, Bankers Trust feels that some information in the case given out by Steven Holley perhaps included some serious libel and could really do them irreparable harm. Why is that fear so incomprehensible to BUSINESS WEEK? Why can't BUSINESS WEEK figure out that part of this "democracy" includes the rights and respect of privacy, whether the entity is a person or a corporation?

William S. Simon  
Atlanta  
WSS1@aol.com

We cannot allow the courts to censor the press and allow violations of the First Amendment. The people have a right to know. Your recent article on the Dow Corning breast implants might have been written earlier if the courts had not sealed the lawsuits that Dow Corning fought early on.

John Gordon  
Cedar Grove, N.J.

## BREAST IMPLANTS: WHO BEARS RESPONSIBILITY?

The experience of Colleen Swanson described in "Informed consent" (Cover Story, Oct. 2) is duplicated in my wife's case. She has Dow Corning implants. She utilized the services of Dr. James

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# How Does the World's Most Powerful Software Company Create Technology, Shape Markets, and Manage People?



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## Microsoft SECRETS

Michael A. Cusumano  
and Richard W. Selby



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## Readers Report

Baker, and she has all the symptoms expressed by Colleen. In fact, they started 30 days after the implants and continually increased in severity. We don't know if it's MS, lupus, or what. We just know the symptoms are the same, and it has robbed my wife of the lifestyle that she had prior to the implants.

This article reflects the extent that Corporate America will go to to make a profit. The question that needs to be resolved is how to make this segment of Corporate America responsible for having destroyed Colleen's life, my wife's life, and the lives of thousands of others. The answer is to make them pay with real dollars, to every victim. This is the only transplant they understand.

William Lord  
Mt. Airy, Md.

I was immediately drawn to your cover story regarding John and Colleen Swanson. Understanding that the published excerpt is but a fraction of the whole picture, something doesn't smell right in light of Swanson's status in the field of corporate ethics.

If we are to assume, conservatively, that Swanson held a personal conviction that silicone breast implants posed health concerns to women on or around September 18, 1991, the date of his request for recusal from work connected to breast implants, it is difficult to reconcile his course of action over the next two years. Perhaps Swanson felt he could do more good working on the inside, gathering information about the potential risks of implants. This information might have led to earlier detection of similar symptoms in others. However, it appears Swanson did nothing more than sit idly by until he could retire and collect royalty payments from his collaboration on the book from which your article is excerpted.

I appreciate the "real life" conundrum that Swanson faced. But it is in situations like this that our reasoned discretion and ethical judgment are called upon. While known for what he did in the area of corporate ethics, Swanson's legacy may lie in what he failed to do.

Andrew Nardone  
Bridgeport, Pa.

While many popular publications are printing public-relations propaganda put out by the breast implant manufacturers, your article did not follow that line.

I, like Colleen Swanson, am an implant victim. I've suffered for years from illnesses caused by the implants. The makers didn't do adequate tests and even failed to notify me when they

had information that their implants were being associated with various illnesses. In their arrogance, they denied me the opportunity to be explanted years ago.

Marilyn W. Hall  
Hosier, Va.

### MEDICARE ENROLLEES DON'T NEED A FLEEING

Regarding your article "How to Shop for Medicare" (Social Issues, Oct. 2): Insurance companies and their agents are salivating over the prospect of phony vouchers in the hands of the elderly for the purpose of buying insurance.

Your author's fantasy that "the elderly would shop among dozens of forms of insurance companies, all of doctors, HMOS, and other managed care providers" is just that. I suggest that before your reporter writes further on the subject, he interview insurance department examiners to find out how insurance sales to the elderly work in the real world.

Roger P. Estes  
Estes Park, Colo.

One of your suggestions is that seniors use vouchers to buy basic insurance or to turn into cash and use it in tax-free Medical Savings Accounts.

I am a volunteer who has been helping other seniors on Medicare-related matters, and based on my experience, I can tell you that the 70-, 80-, and 90-year-old, for the most part, will be able to cope with the marketplace to carry out the above recommendation, nor should they.

Morris Iverson  
New York, N.Y.

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## FIDELITY'S WORLD

The Secret Life and Public Power of the Mutual Fund Giant

By Diana B. Henriques  
Scribner • 416pp • \$26

# AN 800-POUND GORILLA ON THE LOOSE?

**W**ith its 223 mutual funds and \$346 billion in assets, Fidelity Investments has the ability to exercise enormous control over the performance of individual stocks, big chunks of the market, and, increasingly, world markets. No wonder many investors have an intense curiosity about how the company works—and deep-seated fears about how it uses its power and whether this huge, loosely regulated fund machine could implode.

Thus, many will be intrigued by *Fidelity's World: The Secret Life and Public Power of the Mutual Fund Giant*, written by Diana B. Henriques, an investigative reporter for *The New York Times*. As the first book of any import about Fidelity, it warrants a look by anyone interested in mutual funds and the role of the industry's biggest player.

Unfortunately, the book offers little insight into what really takes place inside Fidelity. What redeems *Fidelity's World* is its extensive reporting on the history of the mutual-fund industry and the lax regulatory system that has developed since the 1930s. These topics hardly make for riveting reading. But they are central to the book, since the crux of Henriques' argument is that Fidelity has grown so large and secretive that the U.S.'s archaic securities laws no longer adequately protect investors. It's an intriguing idea—but first, some background.

*Fidelity's World* was written without the cooperation of Fidelity employees, the author tells us. Although she provides no explanation for this fact, her past reporting offers a clue. Henriques' clips include several articles critical of Fidelity, including a 1991 *Times* story that documented the questionable investing tactics of a former Fidelity employee, Dorsey R. Gardner, who managed aggressive private offshore funds. Although Fidelity officials decline to comment on the book, they likely saw

little to be gained from cooperating.

So the book's hostile tone should come as no surprise. "For much of its life," the author writes, "Fidelity has managed to glide smoothly across the cracks between its public image and its internal reality: Its image as a sagacious money manager and its compelling determination to sell funds no matter how risky or ill-conceived they may be..." Henriques has chronicled every misdeed she could uncover, and there's hardly a sympathetic word in the book.

The first chapter sets the tone with a riveting account of Fidelity's role in the 1986 takeover battle at Kaiser Steel Corp. With control of nearly a third of the company's preferred shares, Fidelity and its senior executives, including Chairman Edward C. "Ned" Johnson III, as well as Johnson's friend and adviser, Joshua M. Berman, a New York lawyer, are shown as key, if inept, actors in a hard-fought proxy battle. The story illustrates a fact not well understood about Fidelity: This giant investor is sometimes an aggressive behind-the-scenes player, too. Of Johnson, she observes: "Not since the days of the robber barons... had so much money—other people's money—been controlled by a single individual." But did Johnson actually exercise this power to the detriment of stockholders? Although Fidelity lost money on Kaiser, Henriques doesn't convince us that the company acted irresponsibly.

Still, this chapter provides the book's most compelling reading. Then come long sections of often eye-glazing historical background, followed by a rehash of modern-era misdeeds, including Gardner's rogue investing practices and the activities of two Fidelity employees in

the junk-bond deals of the 1980s. The details are fresh, but most of these series have been well chronicled elsewhere.

The final chapter presents the author's strongest case that Fidelity is out of control. She argues that Fidelity gives its fund managers too much freedom, allowing them to make inappropriate investments. For example, says, several supposedly conservative bond funds invested in Third World debt last year and got burned. As a result of a recent proxy vote, Fidelity's Magellan fund, supposedly a growth-stock fund, may begin investing in commodities and certain types of estate and buying stocks on margin through short sales. What assurance do investors have that Fidelity funds remain true to their charters? "Fidelity," Henriques quotes a Fidelity executive as saying to stockholders.

Clearly, Henriques is appalled by the answer. Fidelity's "funds now are to use investors' money in ways

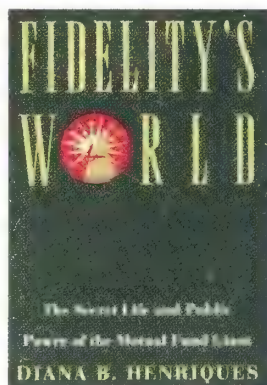
framers of the Investment Company Act [of 1940] would goggle over—who would answer to anyone except the usually compliant investors on the fund boards," she writes. In "an industry whose standards were designed for lapdogs," Fidelity frequently acts like an "800-pound gorilla."

Trouble is, after suggesting scandalous behavior, Henriques has little to reveal. Is Fidelity at the start of a crisis? Perhaps not probably no more so than any other fund company. Henriques correctly identifies potential problems—noting, for example, that investors might flee if Fidelity suddenly starts losing money on investments that shareholders don't think their funds could make. And, in the absence of regulatory reform? After suggesting that there's a dire need for greater regulation, Henriques fails to elaborate.

*Fidelity's World* reveals that there's a lot more going on at Fidelity than stock-picking. But for a book that is meant to shock readers, *Fidelity's World* instead offers reassurance to Fidelity's millions of investors—in the form of the absence of any "secret" scandals.

BY GEOFFREY WATKINS

Smith covers Fidelity from *BUSINESS WEEK's* Boston bureau.



## HENRIQUES CLAIMS LAX LAWS LET FIDELITY RUN WILD—BUT SHE DOESN'T PROVE HER POINT

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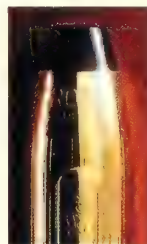
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STEPHEN H. WILDSTROM

## MAKING PC FLICKS FLICKER-FREE

Ever since multimedia "movies" started showing up on personal computers a couple of years ago, I've been underwhelmed. Somehow, a jerky, postage-stamp-size image of some exciting scene, explaining the Internal Revenue Code, his lips out of sync with the sound, just didn't add much to the experience of filling out a 1040.

When I saw clips of Arnold Schwarzenegger in *Lies* on a new IBM ThinkPad 760CD. The screen was filled with the motion. It was smooth, flicker-free motion was as good as a VCR reeling—and the sound was in sync with the motion.

**JSM.** The difference is a technology called MPEG, and we're going to be seeing and hearing a lot more about it as it makes its debut on consumer-market PCs this fall.

Initially, MPEG announced "em-peg") technology will combine with 3-D graphics (a topic I'll cover next week) to add realism to movies. But like digital sound on CD-ROM drives before it, MPEG will quickly migrate to games and entertainment to a broad variety of applications, including interactive training videos and virtual reality catalogs. There are many uses we can't even begin to see yet.

MPEG was developed by Motion Pictures Experts Group, an international standard-setting panel. The format provides for drastic shrinking of images—and a standardized way of decoding

them. Data compression is the key because the worst bottleneck in today's computers is moving data, not processing it. CDs were designed to move 1.5 million bits per second, and faster drives have boosted the speed to about 9 million BPS. But your computer must be able to swallow 150 million BPS to



put smooth action on the screen. Adding broadcast-quality color and resolution can double or triple the demand. MPEG fills the gap by reducing the volume of data by more than 95%.

There are two approaches to the compression process, with significant differences in what you see. Software decompression is cheap, but it relies on your computer's processor chip to do the work. A Pentium chip can handle the load, but only at the expense of other things it might be doing. Software-only MPEG is built into Packard-Bell's current line of home computers.

The next release of Microsoft's Windows 95 will include both MPEG and a new version of Indeo, Intel's rival software video-compression standard. You can also download MPEG software from the Internet and online services.

**ONLINE MOVIES.** To really see MPEG show its stuff, you need hardware decompression, which uses special chips to take the load off the central processor. Right now, it's a fairly expensive add-on: MPEG boards from Creative Labs, TeleVideo, Boffin, and Sigma Designs run \$250 to \$300. But prices are about to plunge as a mass market develops for the technology. Compaq Computer Corp. is building hardware MPEG into

its new Presario desktops and LTE 5000 laptops. Hardware companies such as Chromatic Research are designing specialized chips that will handle a variety of multimedia tasks, including MPEG, at a fraction of the cost of today's systems.

Right now, MPEG applications consist mainly of games and online files, such as satellite weather photos. But software publishers are ready to provide new content as the hardware becomes pervasive and MPEG movies replace the low-quality videos now found on CD-ROMs.

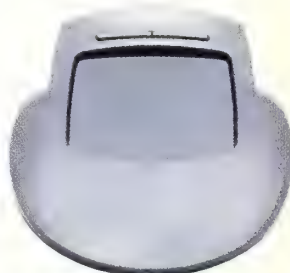
A further boost will come from the recent agreement by entertainment and consumer-electronics companies to use a new standard for high-capacity CDs. Together with even more efficient MPEG compression, the new format could hold an entire feature film on a single 5¼-inch disk—and turn your computer into a really expensive video player. The whole history of the PC industry, however, has been that the basic technology comes first and the applications follow quickly. So just stay tuned—literally.

## BULLETIN BOARD

### CURSOR CONTROL

#### A MOUSELESS PAD

If moving a mouse to make things happen on your computer screen doesn't seem quite natural, you might want to try the Touché Touch Pad from International Technology Associates (800 223-6433). You control the cursor by moving your finger along a



smooth, 2-by-2½-inch surface and tapping to simulate the effect of mouse buttons. I found fine-motion control on the \$59 Touché device considerably easier than earlier touch pads, such as the ones used on Apple PowerBook laptops. Touché is available in versions for PCs or Macintosh.

### MEMORY

#### ALWAYS QUIT WINDOWS

Is your computer's hard drive mysteriously filling up? If so, perhaps you're not leaving Windows properly. Windows creates a number of temporary files, usually in your \dos directory under Windows 3.1. If you turn off your computer without shutting down Windows, these files never get deleted. The answer is to select File/Exit Windows or press Alt-F4 in the Program Manager to quit. A graceful exit is even more important if you use Windows 95. Unless you use the shutdown command—found on the Start menu—you may fail to save important configuration data when you power down.



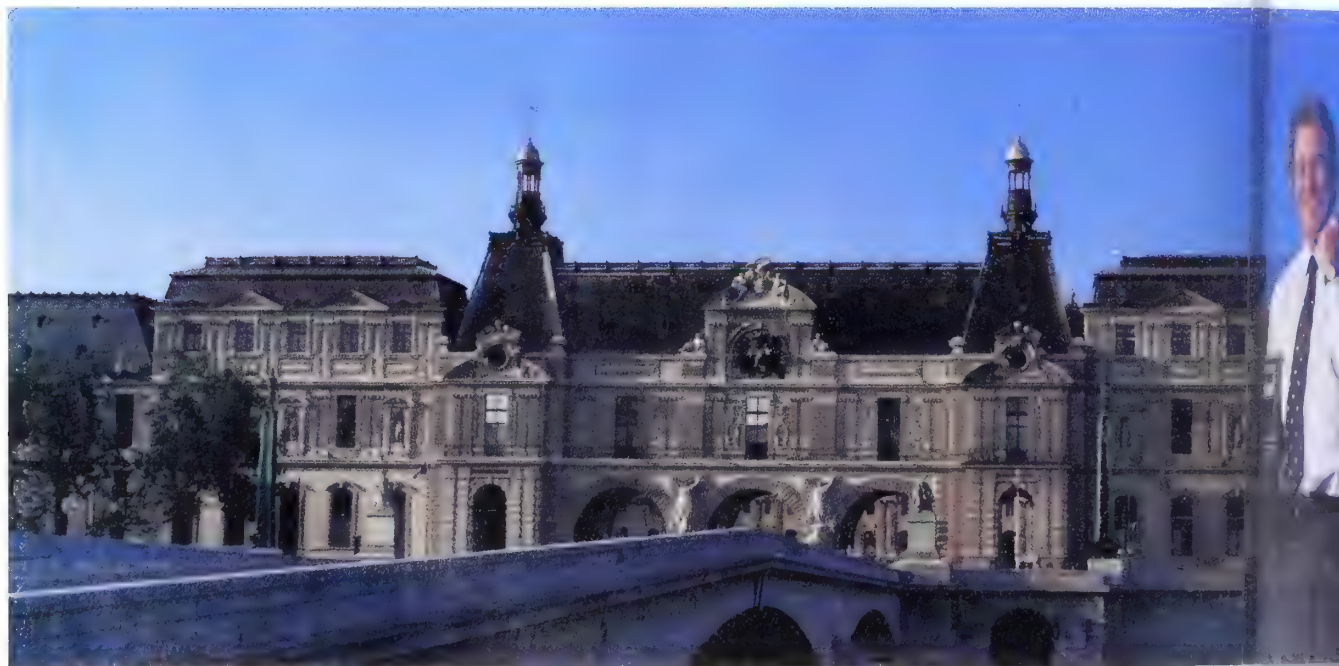
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BY RUDI DORNBUSCH

## THE ECONOMY'S DIRTY LITTLE SECRET



**PUMPED UP:**  
Official stats exaggerate inflation. Fixing them would be politically risky, but economically wise

**I**nflation in the U.S. has been low for more than a decade—3.6% since 1985—which is half the rate of the previous 10 years. And it may soon fall even further. Yet this additional decline in inflation won't result from superior Federal Reserve policy, highly competitive markets, or a soft economy. It will come from an adjustment of the way the consumer price index (CPI) is measured. With new and better measurements, inflation would fall somewhere between 0.7% and 2%.

Unfortunately, the shift to more accuracy is highly controversial. The overstated official inflation rate has helped some groups benefit at the expense of others, including the Treasury Dept. Everyone from senior citizens to labor unions would initially decry it, but improving the exactness of data is good policy because it allows the economy to collect a bonus.

The overstatement of inflation in the official CPI measure stems from some obvious causes. Over time, people's consumption patterns change as they substitute relatively cheaper goods for expensive ones. But computation of the CPI "consumption basket" tends to lag behind the change. Too much weight is given to high-priced goods over relatively cheap ones. It takes periodic rebasing of the basket to eliminate the bias.

**SMARTER SHOPPERS.** In addition, the quality of most goods improves over time. This quality improvement must be reflected in the downward adjustment of inflation, and, indeed, allowance is given. But it's far too little, since quality improvement is so dramatic, what with new materials, better cars, and far better computers. Also, people are serious discount shoppers these days. On Fifth Avenue, it is called an "accommodation," elsewhere simply a sale. Ideally, the CPI would capture this by collecting the discount prices—but often the list price, not the transactions price, gets into the sample. This, too, overstates inflation.

The opposition to cutting the CPI is strictly political. The official inflation measure is used in three key places. In the Social Security cost-of-living adjustment, it has led to continued overpayment. Because true inflation is less than official inflation, real payments to the recipients are steadily rising. Seniors have been overpaid by billions of dollars over the past decade.

Also, taxpayers have been getting a break

by being asked to fork over too little. If brackets are indexed, and official inflation pushes the thresholds of those brackets up too much, allowing the middle class to escape more serious tax bite. And finally, the cost-of-living adjustment in labor contracts is too high. That reduces corporate profits.

It is clear that the President and Congress are not eager to bite the CPI bullet: Taking more money from the middle class and passing it to the elderly is a prescription for disaster. Telling workers they are overpaid when in fact they feel squeezed seems politically unwise. Yet the right thing is to use true inflation. Congress and the President could then rearrange around and allocate the harvest by introducing middle-class tax cuts, reducing capital gains taxes, or whatever is the fashion of the day. They might even ease up on the most extreme budget cuts now on the table. There is simply no reason to keep using the wrong numbers.

**GIFT HORSE.** The bonus for doing things right is the potential for a period of far easier money. The Fed is constrained by headline inflation that focuses on the official CPI rate rather than the facts. Everybody knows there is virtually no inflation in America, yet the Fed must follow by what the official numbers show. Low inflation on the front page means lower interest rates in no time. In Germany, this happened when a revision of the CPI pushed inflation down half a percentage point; the Bundesbank responded with a half-percentage-point cut in rates—with possibly more to come. By cutting the current CPI in half, the Fed would be able to push down rates to 4%. There would be an economic boom anywhere else in the world.

Of course, the adjustment is simply a bonus and not a license for perpetual unbounded growth. But who minds a bonus? The sustained economic growth will improve the budget thereby also lowering interest rates.

Using a better CPI is not the panacea that will turn America into a monetary and fiscal paradise. But it would unleash enough favorable effects to make it well worth the effort. When President Clinton introduced a stimulus budget package at the outset of his term, low interest rates and vigorous growth followed in no time. The President should muster the courage for another round rather than yield to the shortsighted tantrums of the overpaid and undertaxed.

Rudi Dornbusch is professor of economics and management at Massachusetts Institute of Technology

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INSURANCE & INVESTMENT



BY GENE KORETZ

## THE 'TOP LINE': NOT TOP DRAWER

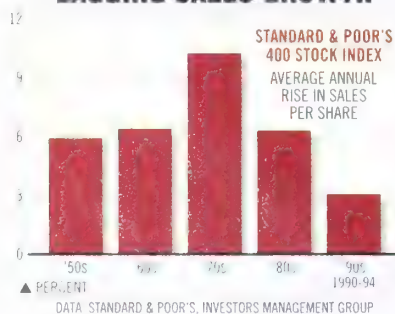
Will scant sales rein in profits?

According to economist James W. Paulsen of Investors Management Group in Des Moines, a paradox is troubling Wall Street and Corporate America in the 1990s—one that raises worries about profit growth in the years ahead.

The paradox is the absence of a trend that has contributed to every other profit boom since the war: "top-line" growth, or sales increases. Nominal gross domestic product, a good proxy for the economy's total sales, has grown at a scant 5% annual rate in the 1990s, its slowest pace since the Depression. Sales chalked up by S&P 400 companies have advanced at an average of just 3.1% a year (chart), suggesting that real sales gains have been slim.

So far, business has been able to thrive in an environment of sluggish top-line growth, observes Paulsen, by adopting a number of cost-cutting strategies. Restructuring and downsizing

### CORPORATE AMERICA'S LAGGING SALES GROWTH



have eliminated fat in employee ranks. Hefty investment in technology has made remaining workers more productive. And companies have replaced high-paid employees with lower-cost temps, part-timers, and contract workers.

Such tactics in turn have heightened insecurity among workers—enabling business to enforce wage restraint and to boost the share of national income claimed by profits. But they have also fostered resistance to higher prices among consumers and thus contributed to the lack of top-line growth that helped touch off the cost-cutting drive in the first place.

Unable to raise prices, businesses in-

sist that they must continue to trim costs and become even more efficient. But Paulsen wonders how much further profits can be enhanced by "below the line" cuts. And he worries about diminishing returns from upgraded technology. "After six or seven years of downsizing," he asks, "how much profit juice is still left to squeeze out?"

In sum, Paulsen thinks that much of the profit surge of the 1990s resulted from one-time cost-cutting tactics that are losing their potency. If this is so, then profit growth is unlikely to be sustained without enhanced sales growth.

With the sluggishness in overseas economies, weakening exports, scant U.S. macroeconomic stimulus, and consumers as budget-minded as ever, "the critical question," he says, "is just where that sales growth will materialize."

## WEIGHING THE R&D TAX CREDIT

Its overall impact is modest

Should Congress extend the recently expired "temporary" 14-year-old research and development tax credit, make it permanent, or let it pass into oblivion? Ideally the answer should depend on the credit's effectiveness. But as a recent report by Congress' now-defunct Office of Technology Assessment makes clear, effectiveness depends on the goals sought. The OTA says the credit produces about \$1 in additional R&D outlays for each \$1 of lost tax revenue. Thus, it is clearly effective in boosting corporate R&D spending at the margin.

But the agency also notes that some experts argue that government sponsorship of R&D should focus on areas that the market may fail to support: basic research that has long-term pay-offs or the efforts of small entrepreneurial firms in such fields as biotechnology and information technology. From that standpoint, the credit seems less successful. Some 70% of tax-credit funds are claimed by large companies—with more than \$250 million in assets. Companies with less than \$10 million in assets account for a mere 11% of claims.

In truth, the credit, which costs the government \$1 billion to \$2 billion a year, plays a very small part in the nation's R&D effort. It accounts for only 2.6% of total federal R&D funding and just 1.6% of all nonfederal business R&D spending—surprisingly small potatoes, in view of the heated debate it has generated over the years.

## THE POLITICS OF DEFICIT-CUTTING

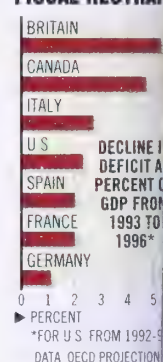
It's harder when times get tough

The industrial world's swing toward deficit reduction could be impeded by a political backlash sparked by current slowdown in economic activity. As measured by the Organization for Economic Cooperation & Development, Britain's deficit will fall from 7.9% of GDP in 1993 to 2.6% next year, a drop amounting to 5.3% of GDP. Aside from Japan, which has turned to fiscal stimulus to stave off a deflationary spiral, other industrial nations are following suit (chart).

Such moves are not only inspired by fears that aging populations will add to the weight of bloated social-welfare spending, but in Europe are also the prerequisite for a common currency. They are reinforced by the discipline imposed by deficit-wary financial markets.

The problem is that industrial economies are now weakening—in part because of the fiscal restraint already in track—and unemployment is rising. If economic growth rebounds, the pressure to delay cuts in social spending is likely to mount.

### A GLOBAL SHIFT TOWARD FISCAL RESTRAINT



## A SMIDGEN OF BLACK PROGRESS

Poverty dips, and income rises

Although U.S. median household income was stagnant in real terms last year, the strong economy lifted living standards of poor and lower-middle-class black Americans for the first time since the late 1980s.

According to the Census Bureau, the overall poverty rate dipped to 15.1% in 1993, but among blacks the drop was a sizable 2.5 percentage points, to 30.6%. Of the 1.2 million decline in the number living in poverty last year, blacks accounted for nearly 60%. Meanwhile, the real median income of black households rose a modest 5%, to \$21,027, in 1994—the only gain posted by any racial or ethnic group.



MES C. COOPER & KATHLEEN MADIGAN

## THE BAD NEWS FOR JOBS IN THE GOODS SECTOR

**U.S. ECONOMY** If you want to know what's happening in the economy now, take a look at the split between goods and services in the September employment report. Jobs in the private service sector increased by a healthy 100,000. But goods-producing industries—mining, construction, and manufacturing—lopped off 18,000 jobs. Manufacturers alone cut their payrolls by 32,000. The job gap says loads about the cyclical forces at work right now. Last year, gross domestic product rose more than 7%, the fastest growth in a decade. But by early 1995, demand for goods was getting the strong headwinds from the Federal Reserve's interest-rate hikes, and inventories suddenly got top-heavy, forcing production cuts.

### HAT'S WEIGHING DOWN JOB GROWTH



is that, heading into the fourth quarter, stock prices appear to be in much better shape than they were in the spring, clearing the way for manufacturers to pick up output.

**HOLD THE HALLELUJAH.** There also are structural forces restraining the economy's general manufacturing especially. Ongoing pressure to restructure and enhance competitiveness will mean layoffs of factory workers—more so than service-sector employees—will bear the brunt of smaller pay hikes and greater job insecurity (chart).

Even in a growing economy, layoffs at big manufacturing companies will continue to capture the spotlight, dragging down consumers' spirits whether or not they work in manufacturing. With profits set to rebound from a strong performance through the first half of the year, the squeeze on payrolls and wages may intensify. Be sure, services are also feeling the heat, but less so in manufacturing. That's because service producers retain a bit more pricing power. Annual consumption in services is currently running at 3.3%, while goods inflation is only 1.6%.

On balance, the September job report says the economy is slowly improving. The nation's payrolls rose by a modest 121,000 workers. Job gains in the third quarter averaged about 140,000 per month, up from about 80,000 in the second quarter. The unemployment rate held at a low 5.6% of the labor force. Also, the workweek in the nonfarm sector increased by six minutes, to 34.4 hours, and average hourly pay rose by 0.3%, to \$11.52—suggesting good income growth.

Judging by jobs alone, though, the manufacturing sector took a turn for the worse in September. Payrolls had shown signs of stabilizing in August, but an originally reported increase of 12,000 workers—the first rise in five months—was revised to essentially no gain at all.

Throughout this expansion, however, the factory workweek and overtime hours have said more about the trend in manufacturing output than has employment. Indeed, during the first three years of the expansion, factory payrolls fell nearly 2%, even as output rose more than 14%. Only by 1994 did factories start adding workers. But in the past six months, manufacturers have laid off half of those 400,000 new hires.

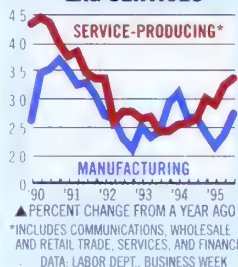
The six-minute rise in the factory workweek in September—including a 12-minute increase in overtime—coupled with the big 1% advance in August factory production suggests that manufacturing output is now turning up, as excess inventories are virtually all worked off. Factory inventories in August remained flat, even with the jump in output.

**THE PROBLEM:** Even as factory output picks up, factory pay gains are lagging overall wage growth generally, and service wages in particular. Last quarter, factory wages rose 2.7% from a year earlier while service pay grew 3.4%, based on a weighted average of service industries compiled by BUSINESS WEEK. The monthly job report does not aggregate hourly pay among service-producing industries.

The numbers show that wage growth in manufacturing has waffled between 2% and 3% in recent years, but service pay is in a clear uptrend and is now growing at its fastest pace in four years (chart).

Why the split? Competitive pressures, in addition to past Fed tightening, are hitting manufacturing pay

### PAY GROWTH: FACTORIES LAG SERVICES





# Business Outlook

hard relative to services, where the squeeze is less intense. Goods producers are more vulnerable to imports, which continue to grab an ever-larger share of U.S. markets, so goods-producing jobs are more exposed to outsourcing and foreign labor.

One irony in all this is that real wages in the factory sector, which has made tremendous advances in productivity, continue to fall. Meanwhile, real service pay, adjusted for inflation by the core consumer price index, is up 0.5% during the past year. Modest, yes, but that's still the fastest pace in more than a decade.

The implication for the outlook is that despite the weakness in factory employment and pay, service-sector gains will help to buoy consumer spending. Private-sector services employ three-fourths of all private-sector workers.

The September increases in hourly pay and the workweek meant that overall weekly earnings rose 0.6%. Combined with the month's job gains, that means personal income for the month and for the third quarter rose at a healthy clip. Income growth will continue to support domestic demand in coming months.

**IN ADDITION, MANUFACTURERS** will be keeping a keen eye on foreign demand. Right now, though, Dun & Bradstreet reports that factories are becoming less upbeat about export markets.

A Dun & Bradstreet Corp. survey of 5,000 U.S.

companies shows that manufacturers' expectations for exports through mid-1996 are sharply lower. Nearly 49% of exporters expect higher foreign demand, a decline of some 12 percentage points from last year's reading. D&B says uncertainty about economic stability in Japan and Mexico is cutting into expectations.

The latest world economic forecast by the International Monetary Fund suggests that, on average, global output will rise modestly in 1996. Only Latin America will provide a better growth climate in 1996 than in 1995. Growth in Europe will about match its 1995 pace, while growth in Southeast Asia will cool off a notch (table).

However, IMF forecasts tend to be overly upbeat. In particular, growth in Europe may be limited by weakness in domestic demand, which has not come along as it was expected to in the wake of an export-led recovery. Weaker growth worldwide will bear out the exporters' downbeat sentiments. But with foreign sales so important to the bottom line, this is one time that they would not mind being wrong.

## GROWTH PROSPECTS IN FOREIGN MARKETS

|                | GDP GROWTH |      | SHARE        |
|----------------|------------|------|--------------|
|                | 1995       | 1996 | U.S. EXPORTS |
| CANADA         | 2.2%       | 2.7% | 22           |
| JAPAN          | 0.5        | 2.2  | 10           |
| BRITAIN        | 2.7        | 2.9  | 5            |
| FRANCE         | 2.9        | 2.7  | 2            |
| GERMANY        | 2.6        | 2.9  | 3            |
| ITALY          | 3.0        | 2.8  | 1            |
| EUROPE         | 2.9        | 2.8  | 21           |
| LATIN AMERICA  | 1.8        | 4.0  | 16           |
| SOUTHEAST ASIA | 8.7        | 7.9  | 13           |

DATA: IMF, COMMERCE DEPT., BUSINESS WEEK

## ITALY

# INFLATION MAY BUST THE BUDGET

**A**lthough Italy's upturn paused in the spring, the setback does not dim the economy's prospects. But it also doesn't improve the poor inflation outlook—a hitch in the latest budget plan.

Real gross domestic product fell at a quarterly rate of 0.4% in the second quarter, the first decline in 1½ years. The drop resulted from an inventory correction, after two quarters of rapid stock building. Domestic demand and exports grew a sturdier 1.5%.

Even with the drop, second-quarter GDP was 2.9% higher than a year ago—in line with the official 3% growth forecast for 1995.

Thanks to a weak lira, the export boom continues. Real exports

rose 4.2% in the second quarter, and 17.6% above year-ago levels. Italy's trade surplus for the first half widened by 15.5% from the same period in 1994.

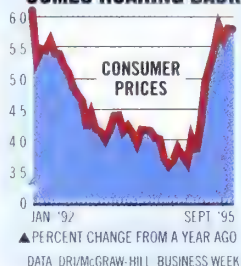
Excess inventories have crimped industrial output a bit. Production was up 4.5% in the year ended in July, slower than its 6.5% gallop in May. Still, as inventories return to leaner levels, output and economic growth will rebound.

Amid growth, Italy can concentrate on its top problem, the public deficit. The government released its draft for the 1996 budget. To hit the deficit target of 5.8% of GDP, the plan calls for 17 trillion lire (\$10.6 billion) in new revenues,

and 15.5 trillion lire in spending cuts. Italy's structural primary surplus, which excludes the budget's huge interest payments, will rise to 4.3% of GDP. The plan increases spending in the south, which has not benefited from the export surge. Indeed, the jobless rate in the southern region stood at 20.7% in July, compared with 11.7% nationally.

The overall plan, however, hinges on inflation of about 3.5% in 1996. But in September, consumer prices were rising at a 5.8% pace (chart), and private forecasts put 1996 inflation well above 4%. That means interest rates and debt payments will overshoot their targets. Still, the hope is that pressure from other European nations, which are striving to rescue the monetary union, will force Italy to make some hard fiscal decisions.

## ITALY'S INFLATION COMES ROARING BACK



Total multi-vendor chaos incompatible protocols inflexible systems

inaccessible information limited scalability

ends here.

Network

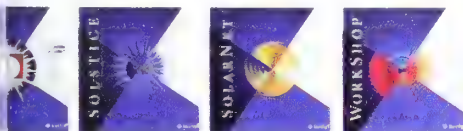


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CORPORATE PROFITS

# SPOOKED ON THE STREET

Investors are jittery over profits, but the economy is far from spent

Is the economic expansion over? Investors fear the worst, as companies from industrial stalwarts 3M and Caterpillar to high-tech goliaths Motorola and Novell to auto giant Chrysler fail to meet Wall Street's earnings predictions for the third quarter. Little wonder that stock markets have been jittery, posting precipitous drops on record volume, then clinging to fragile recoveries.

Is it time for investors to circle the wagons and start stuffing cash into mattresses? Hardly. This recovery isn't over yet. Gross Domestic Product during the third quarter grew around 2.2%, economists agree, above the 2% growth most predicted. And a 3% GDP increase in the fourth quarter isn't out of the question, says 3M Corp. economist John McDevitt. Among the positive signs: Housing starts and consumer purchases continue to tick upward. "People are looking for evidence that the cycle is ending, but I see no good reason why it should," says Jeffrey T. Grade, chairman of Harnischfeger Industries Inc., a Milwaukee-based machinery company.

Other than healthy skepticism—and the gnawing memory of the October, 1987 crash—there isn't much basis for the market's current jitters. Housing

starts, fueled by 30-year fixed-mortgage rates of 7.6%, should continue strong into 1996. That should boost the earnings of construction companies, appliance makers, and machinery manufacturers. And spending on new plant and equipment should spurt to 14.5% this year—the third straight year of double-digit growth—with an increase in the high single digits likely next year. Even some retailers are cheery. Just last spring, Sears Roebuck Chairman Arthur C. Martinez was planning for a conservative Christmas season. Now, he says, he's "optimistic."

Why is business so optimistic? Many executives credit Federal Reserve Board Chairman Alan Greenspan with engineering a soft landing for the economy that could stretch well into 1997. While profits may not rise as fast as earlier in the cycle, there's no reason why they should fall precipitously either, they say. Aluminum Co. of America Chairman Paul H. O'Neill, whose company re-



ported record third-quarter earnings of \$226.4 million on Oct. 6, way above analysts' expectations, says he "expects earnings to stay good." Both head Richard C. Notebaert, chairman of Chicago-based Ameritech Corp., are buoyed by the prospect of what Notebaert terms "steady, constrained, economic growth."

So why the chill on Wall Street? Certainly, the economic expansion is slowing somewhat, helping to cut expected growth from 36.3% in 1993's third quarter to an expected 16.1% in 1994.





## SHIPPING SCOTCH TAPE 3M's inability to hit growth projections has little to do with the economy—but don't tell Wall Street that

profits is overstated. Dozens of companies, including Morgan Stanley, Oracle Systems, and General Mills, have hit or beat expectations, laying waste to the notion of a broad weakening. As for companies that didn't beat estimates, blame Wall Street, some say. Peter J. Canelo, chief investment

strategist for NatWest Securities Corp., says many forecasts were just too aggressive. "Analysts got all puffed up" by surprise profit increases in the second quarter, he says.

**NOT GOOD ENOUGH.** Just look at Motorola Inc. On Oct. 9, it announced that its net income rose 30% in the third quarter, to \$496 million on sales of \$6.9 billion. But that wasn't good enough: Analysts expected a 35% increase. Neither the company nor the economy were to blame, though. The cellular-handset market simply grew less quickly than in previous quarters, largely because telecom companies didn't offer discounts steep enough to attract new subscribers.

In fact, in some cases, companies have been singled by flare-ups in a competitor's results. In mid-September, for example, Caterpillar Inc. announced that higher-than-expected inventories would force it to slow production. Wall Street, fearing lower profits, knocked Cat's stock price down 20%, to around \$52. The sell-off quickly hit rival Case Corp., too. But Case Chief Financial Officer Theodore R. French says that Case's construction equipment orders are up over 30% this year and that inventories are in great shape. "We're pretty optimistic about things," he says. "We can't figure the market out."

Even the travails of giant 3M, long an economic bellwether, can't be completely linked to the economy. Late last summer, it announced that slower industrial growth hit second-quarter earnings and could squeeze in the third, too. But the big culprit behind the stumble is the imaging and electronic division, which is being walloped by price competition in computer disks and videocassettes. New-product delays also hurt. Now, Prudential Securities Inc. analyst B. Alex Henderson says 3M may take up to a \$400 million write-down to exit the beleaguered product lines, perhaps as soon as Oct. 25, when it announces third-quarter results. A spokesman says

## Not Good Enough

*s-per-share from year-earlier quarter for S&P 500 companies*

t). Further softening overseas, if economies of Japan and Mexico bounce back, also could hurt. Conversely, many of whom have been taking on heavy debt, are another source of

**TECH TREMOR.** Given those signs, investors are taking profits rather than waiting to see if a downturn develops. The shiver that went through high-tech stocks on Oct. 9 is a good example. The NASDAQ Composite Index slid as mutual-fund investors sold off holdings, concerned that the tech

boom is playing out. At the heart of their worries: News that BMC Software and Apple Computer, in addition to Novell and Motorola, would have earnings disappointments. "People are nervous," says James K. Renck, portfolio manager at the \$1.2 billion Merrill Lynch Technology Fund. With unrealized profits on many tech investments at 100%, holding steady is nerve-racking. And the nail-biting isn't over yet. Intel, Hewlett-Packard, and Texas Instruments have yet to report.

In general, though, the anguish over



the company is "looking at a broad range of options," but has no timetable.

Most experts expect troubled sectors to bounce back before yearend. For one, analysts predict a comeback by the auto industry, where Chrysler Corp. on Oct. 11 posted earnings of \$354 million in the third quarter, down from \$651 million last year. "Business isn't great," admits Wertheim Schroder & Co. auto an-

alyst John Casesa, "but it isn't terrible either." Indeed, in this quarter, he expects the Big Three to collectively post net earnings of over \$3.3 billion. Anticipate the same scenario for many tech companies: Chipmaker Intel, modem manufacturer U.S. Robotics, and computer maker Dell are all looking at sales and earnings increases well into 1996.

Perhaps what the pessimists have

underestimated most is the resilience of an economy goosed by corporate cost-cutting and productivity initiatives, combined with patient Fed policy. The optimists are running for cover now, to give them time. They are likely to get back to gun-slinging any day now.

By Kevin Kelly in Chicago, with Stephen Baker in Pittsburgh and Suzanna Woolley in New York

## COMMENTARY

By Michael J. Mandel

### GREAT THEORY... AS FAR AS IT GOES

**F**ew of his peers would deny that Robert E. Lucas Jr., winner of the 1995 Nobel Memorial Prize in Economic Sciences, deserves the award. Indeed, Lucas, a professor at the University of Chicago, was this year's top choice in the Nobel prize betting pool run out of the University of California at Berkeley.

The reason? Starting in the mid-1970s, Lucas and his followers virtually demolished the Keynesian macroeconomics that had prevailed during the post-war era. Activist economists had believed that government could reliably affect the economy with fiscal and monetary policy. But Lucas argued persuasively that workers and companies have "rational expectations": They anticipate the government's actions in a way that makes intervention less effective. For example, the goal of an investment-tax credit

may be to give a quick boost to capital spending. Yet the theory of rational expectations says that rather than boosting investment, savvy companies will simply delay their pending plant and equipment spending until the credit takes effect.

**REALITY CHECK.** The rational-expectations revolution that Lucas pioneered still dominates economic policymaking. The unwillingness of either the Bush or the Clinton Administrations to take strong measures against the 1990-91 recession and its aftermath reflected the influence of Lucas and his colleagues. In 1994, Federal Reserve Chairman Alan Greenspan suggested that hiking short-term inter-

est rates would hold down long-term rates as investors lowered their views of future inflation, an idea that owes much to Lucas' notion of rational expectations.

Yet as much as Lucas deserves Nobel recognition, the theory of rational expectations has not lived up to its original promise. Unfortunately, models built on rational expecta-

dinary people can understand and forecast the economy, on average, as well as economists do.

But Lucas' theory leads to some unappealing conclusions. For one, it implies that most unemployment is voluntary, even in recessions—a result that would surprise most job-seekers. Similarly, believers in rational expectations often end up

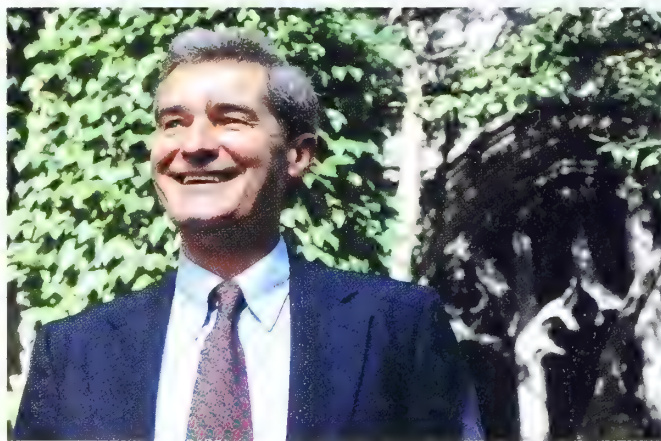
arguing that business cycles are illusions.

**LEFT IN THE DUST.** Another problem: Most economic forecasting models still have a Keynesian core. They predict that the economy speeds up when government spending increases and slows down when interest rates rise despite what the theory of rational expectations says. The result has been an enormous split between the forecasters and the economic theorists.

However, the real tragedy of rational expecta-

tions is that it supports a philosophy of government inaction at a time of rapid economic change. Will technology and free trade create jobs or destroy them? Raise incomes or lower them? What measures will increase growth? All are current conundrums that deeply concern Americans, yet are unaddressed by rational expectations. Even Lucas has shifted his attention in recent years to studying the factors determining long-run growth. Would it were so—that his new area of research be as influential as his old.

*Economist Mandel tracks economic theory.*



**NOBEL IDEA:** Lucas argues that people aren't economic cogs

tions do not reflect the real world as well as the old Keynesian models that they were supposed to replace. Moreover, like the worst type of urban renewal, the proponents of rational expectations have razed without rebuilding—leaving economists without the theoretical tools to deal with issues such as rampant technological change and intense global competition.

To be sure, the idea of rational expectations has tremendous intellectual appeal. Before Lucas, economists viewed workers and companies as automatons, reacting in predictable ways. By contrast, the theory of rational expectations assumes that or-



# WHEN MEDICARE IS RESHUFFLED, WHO WILL HOLD THE AGES?

Consultants will be among the winners, patients won't be

remature infants at Self Memorial Hospital in Greenwood, S.C., are luckier than most. Nurses and doctors hover over 17 tiny incubators in the intensive-care unit, monitoring IVs, thermometers, and the ultraviolet lights that bat jaundice. But Greenwood's preemie may have to be moved 60 miles to another intensive-care nursery if Congress passes a Medicare reform bill. That sounds odd, since Medicare is

igned to serve 37 million elderly and disabled Americans. But Self Memorial President John Dozier says he'll have to close the monitoring ICU nursery and a 13-bed pediatrics unit if he starts hemorrhaging money on Medicare, too. Half of the aged, six-county hospital's revenue comes from Medicare reimbursements. If the GOP's proposed seven-year, \$100-billion cut in Medicare spending comes to

Self Memorial would take a corresponding \$25 million hit.



wouldn't be in any shape to operate the programs we do now unless we're moneymakers," laments Dozier. Congress drafts the legislation reshuffling Medicare, the sprawling health-care industry is toting up the winners and losers. Most hospitals will hurt as the restructuring cuts into revenue bases. As they close down intensive operations and lay off staff, highly paid specialists, patients' ages will suffer. The elderly will face higher premiums and new expensive medical care. Pharmaceutical companies, once the darlings of Wall Street, may lose more. As the elderly—who account for a

third of all drug sales—move into managed-care programs, price competition likely will accelerate. "Some health providers are going to decide we don't need 50 different antibiotics when one or two of the most cost-effective will do," says David B. Friend, director of health-care consulting at Watson Wyatt.

But there will be some big victors in the shakeout. The biggest: managed-care companies, such as health maintenance

## Medicare's Ripple Effect

*Who wins and loses under the GOP reform proposal*

### WINNERS

**HMOs** The GOP plan would push seniors into managed care by reducing traditional benefits. Younger, more profitable patients will switch their coverage first.

**MEDICAL CONSULTANTS** will stay busy advising the industry on cost-cutting and restructuring as well as by evaluating the results of limiting care.

**INVESTOR-OWNED HOSPITALS** For-profit centers have gained by emphasizing efficiencies and profitable procedures. They'll expand as nonprofits close.

**FAMILY DOCTORS** Managed care needs more generalists; they'll compete by forming physician networks.

### LOSERS

**PATIENTS** They'll pay more for medical care because of managed care and cuts in funding. Poor elderly may suffer the most with cutbacks.

**TEACHING, RESEARCH, AND COMMUNITY HOSPITALS** Clinics serving the elderly and poor will see special subsidies cut back. Teaching centers also will lose funding.

**MEDICAL SPECIALISTS** Expensive tests? Marginal surgery? Not anymore: Managed-care groups cut costs by limiting access to such services.

**BLUE CROSS & BLUE SHIELD** As fee-for-service shrinks, companies that administer the current Medicare system will lose out to managed care.



haul would deregulate doctors who form their own group practices and sign up Medicare beneficiaries just like an HMO. The doctors would be exempted from state insurance regulators and from some antitrust laws. "We've been successful even with declining reimbursements from insurance companies because we've been

the new managed-care environment. Consultants already are drawing up new practice guidelines telling doctors when to perform cataract surgery on retirees or provide a cook for an Alzheimer's patient who forgets to turn off the stove. "Change is always good for the consulting business," says Joe Martingale, a partner at consultant Towers Perrin.

**DOCTORS' SPLIT.** For those in health care's trenches, Medicare reform is a mixed bag. Nurses, already hurt by downsizing at cash-strapped teaching hospitals, are in for more bad news as more hospitals look to cut staff. General practitioners will come out winners, as more are recruited to do the work formerly reserved for specialists, such as setting bones or reading X-rays. Doctors' groups, in fact, are split on the GOP plan, though the largest, the American Medical Assn., announced its support on Oct. 10.

Will all specialists lose? Not necessarily. An obscure provision in the GOP Medicare over-

able to cut costs and add efficiencies, and we'll continue that even with Medicare reform," says Roger Garretson, CEO of Orthopedic Physicians Associates, a group of 45 doctors in Seattle.

Even with all the upheaval, most professionals insist the time for changing Medicare is ripe. Indeed with the program's trust fund headed for bankruptcy in 2002 and health care eating an ever larger chunk of the federal budget, the biggest winners may be today's children. "They may wind up with a healthy Medicare program they would have lost otherwise," says Jack Meyer, a health economist. That's as compelling as any reason for everyone to bite the bullet.

*By Paul Magnusson in Washington*

organizations (HMOs), which recruit the elderly from traditional fee-for-service plans. Washington will pay HMOs an average of \$5,100 for each Medicare beneficiary they sign up, so managed-care providers who skim the youngest and healthiest beneficiaries stand to gain windfall profits. But even sicker elders may prove profitable: "We are too big to cherry-pick the youngest beneficiaries, and we don't need to, to remain profitable," says Lawrence P. English, president of Cigna Health-Care, the nation's largest investor-owned operator of HMOs and preferred provider organizations (PPOs).

Also headed for the winner's circle are the consulting firms advising hospitals, insurers, and doctors on how to navigate



## EXECUTIVE SUITE

### INTO THE HARSH GLARE AT ARCHER DANIELS

It's not exactly a debutante ball for Mick Andreas

As he stepped to the podium at the packed annual meeting a year ago, Michael D. "Mick" Andreas moved closer to the spotlight he has studiously avoided for nearly 25 years. Warming to a theme set by his powerful, politically connected father, longtime Archer Daniels Midland Chairman and Chief Executive Dwayne O. Andreas, Mick strongly argued for continued U.S. government price supports for agribusiness giants such as ADM. To many investors, it was a signal that with the eventual passing of the top job from Dwayne, 77, to Mick, the 46-year-old vice-chairman, Archer Daniels Midland Co. wouldn't miss a beat.

Yet on the eve of ADM's Oct. 19 annual meeting, this smooth management-succession plan has been thrown out of kilter. The \$12.6 billion Decatur (Ill.) company is facing an unprecedented assault from federal investigators and angry investors, and the widening controversy threatens to keep Mick Andreas in the harsh glare of the public spotlight for months to come. It's a position to which Mick is unaccustomed. "Outside the ADM complex few know him," says John R. McClendon, chairman of the American

Soybean Association. "He stays inside and runs the company."

Mick now faces a devilish management challenge. Sparked by whistleblower Mark E. Whitacre, the former head of ADM's BioProducts unit fired for allegedly embezzling \$9 million (box), three grand juries are looking into alleged price-fixing by ADM of lysine, high fructose corn syrup, and citric acid. The Justice Dept. also is studying allegations of fraudulent offshore payments to executives. That probe already has resulted in the firing of four senior insiders. Even if Mick



#### MICHAEL D. "MICK" ANDREAS

**BORN** Dec. 30, 1948, Coral Gables, Fla.

**EDUCATION** BS in speech, Northwestern University, 1972

**CAREER** Started as grain trader at ADM, moving through a number of divisions before becoming vice-chairman in 1985; one of four Andreas family members on board. Widely regarded as heir apparent to father, Dwayne, 77, who is CEO

**PERSONAL** Divorced and remarried, four children

DATA: BUSINESS WEEK, WHO'S WHO IN AMERICA

Andreas himself doesn't end up embroiled in the scandal, sources close to the probe expect indictments of other ADM executives, potentially forcing Mick into a fire-fighting job to hold ADM management team together. Meanwhile, troubled that the ADM board is dominated by the Andreas clan, the California Public Employees' Retirement System plans to vote its 0.7% ADM stake against management.

**CONSUMMATE INSIDER.** Investigators refuse to say which executives they're targeting. But a lawyer for one of the executives—Sidney D. Hulse, former vice-president under Whitacre—told his client was told by Whitacre that statements now under investigation were authorized by higher-ups. In a brief phone interview with BUSINESS WEEK, Whitacre wouldn't comment on the statements. But he charged that Mick Andreas "was aware of" the alleged price fixing. Andreas and other company officials refused to comment. ADM

said it is fully cooperating with investigators and has vigorously denied any role in the alleged illegal payments.

It's ironic that ADM is having to grapple with such a public scandal. A speechmaker who is said to dislike public speaking, Andreas avoids the limelight even at trade gatherings. One analyst who has followed ADM for years says he has

### WHAT THE HECK, IT'S A JOB

Fired in August amid embezzlement charges, his legal bills mounting, former Archer Daniels Midland executive and FBI mole Mark Whitacre could use a new job. He apparently has found one.

Whitacre has emerged from weeks of seclusion to report his appointment as chief executive officer of a Chicago area startup biotechnology company, Future Health Technologies. The company, he says, is seeking several patents for its medical products, which he declines to discuss. Its backers, who he says approached him through his attorney,

weren't identified—but they plan a private equity placement next February, with a public offering to come later.

It's intriguing news on several counts—not the least because no one appears to have heard of Future Health. Jack W. Schuler, former president of Abbott Laboratories and a Chicago-area biotech investor, calls the report "really bizarre. If this company has something to do with health care and biotech, I would have heard about it," Schuler says. Other biotech investors are similarly mystified.

Whitacre admits that his company has yet to incorporate—one reason it

fails to appear in the corporate records of all 50 states. In addition, Future Health has no phone listing in the Chicago area. The Cook County Clerk's Office, which registers sole proprietorships around Chicago, has no record of the outfit. Neither does the Securities & Exchange Commission.



**WHITACRE:** A future at Future Health?

Can an unincorporated, phoneless, anonymous operation with no product provide Whitacre with job satisfaction and a steady paycheck? Whitacre apparently

thinks so. "ADM is in the past for me," he says. "I'm trying to put my life back together."

*By Susan Chandler in Chicago*



net Mick or talked to him. Most con- with investors is handled by ayne and Senior Vice-President Mar- L. Andreas, Mick's cousin. consummate insider, Mick rose hough ADM's operating units. He gave an early interest in writing poetry playing the guitar, says a longtime nd, to join ADM right after college as ain trader in Chicago. After a two- stint in Brussels, he settled into atur and rose through the corn and

soy processing divisions. Dwayne's back- ing nearly guaranteed him the top job one day. "Dwayne has run this company like he owns it," one former top execu- tive says. Including Martin and retired President Lowell W. Andreas, Dwayne's brother, family members control 7.5% of the stock, with Dwayne holding 4.7% and Mick 1.2%.

Despite Mick's lofty status, friends in Decatur say he has never lost the com- mon touch. "He's a bit more worldly and

a bit more liberal on social policy than many of us," says sometime golfing part- ner and Decatur businessman John Card- well. "But he's really no different than the rest of us, except he's in the media a lot more now." On the course these days, "we only talk about golf, he never men- tions" the controversy. That's fine on the links. But it will be tough to pull off at ADM's annual meeting.

*By Richard A. Melcher in Chicago, with Catherine Yang in Washington*

## THE INTERNET

### RAIDER ON THE NET Paul Kazarian is on the prowl—online

Paul B. Kazarian doesn't take losing well. In March, the investor, who made his name as chief executive of Team-Oster Co. before being ousted early 1993, was trounced by leveraged out giant Kohlberg Kravis Roberts Co. in a grueling battle to buy Borden. Now plotting his next takeover—of a billion-plus high-tech company he calls it name—Kazarian is determined to And this time he's planning to use a weapon: the Internet.

What may be cyberspace's first takeover battle, Kazarian this fall has launched a site on the World Wide Web that will serve as his command central. Already, he is using it to gather intelligence on possible targets, including the e-mail addresses of their directors and employees. When the battle begins, he plans to send messages to shareholders, board members, employees, and to post information he hopes will sway them to his side. The net is an "awesome" tool for corporate activism, Kazarian says. "It's democracy, free- of speech, and the power to advocate a point of view." Shareholder activists have many ideas. Lens Inc., a Washington shareholder group, recently launched a Web site to disseminate research on corporate finance and, eventually,



#### WEB WARRIOR: First of many?

to wage proxy battles (<http://www.lens-inc.com>). "It's the perfect tool, because any exercise of power requires the control of information," says Nell Minow, a Lens principal. Kazarian's Web site (<http://www.japonica.com>) is more ambitious—even if most of the information posted so far is self-congratulatory patter about Kazarian's past, job listings, and the text of an online confab Kazarian held for fellow Armenian Americans. But the site's ultimate purpose is deadly serious. One section called "director lobbying" lets anyone send messages, private or public, to corporate directors, which then are forwarded to the intended recipients. Kazarian or Web users can also poll institutional investors and conduct research. Says hedge-fund manager Parker Quillen of Quilcap Corp. in New York: "This could change the way institutional investors communicate.... I'm surprised nobody else has done this yet."

Whether it will help Kazarian win his next takeover battle is another matter. The 39-year-old former Goldman Sachs & Co. investment banker has shown a

knack for identifying undervalued companies that are ripe for turnaround. In the 1980s, he was involved in the takeovers of the Chicago & Northwestern Transportation Co. and bike maker Murray Inc. But he did his reputation serious harm while at Sunbeam, where his management team charged that he was abusive. He was accused of throwing objects and harassing female employees, among other things. Kazarian denied the charges, filed a wrongful-termination suit, and won a \$180 million settlement from Sunbeam's largest shareholders.

**POSSIBLE PITFALLS.** His war chest amassed, Kazarian now hopes to reestablish himself in the takeover game. He concedes that the Internet might not have changed the outcome of the Borden contest. The company's board balked at considering his bid, citing his unwillingness to publicly disclose the source of his financing. Still, Kazarian thinks his odds would have improved had he been able to E-mail Borden directors and shareholders.

Perhaps. But Kazarian's plans for using the Net open up a host of potential legal problems. For instance, it is illegal for holders of 5% or more of a company's shares to communicate in advance of a takeover attempt. Online communication with investors could violate that rule, notes Joseph G. Hadzima Jr., a deals lawyer at Sullivan & Worcester in Boston. What's more, a Web-based proxy fight or tender offer might conflict with Securities & Exchange Commission rules requiring full

disclosure of a bid, Hadzima adds. And Quillen says he would be concerned that private communications on Kazarian's Web site could violate insider-trading rules.

Kazarian's response: In a takeover, all communications from his camp will be open. "The beauty of the Internet is that everyone has instant access," he says. *En garde*, cybersnipers. Corporate takeovers could be entering a new era.

*By Geoffrey Smith in Boston*

## What's on Kazarian's Web Site

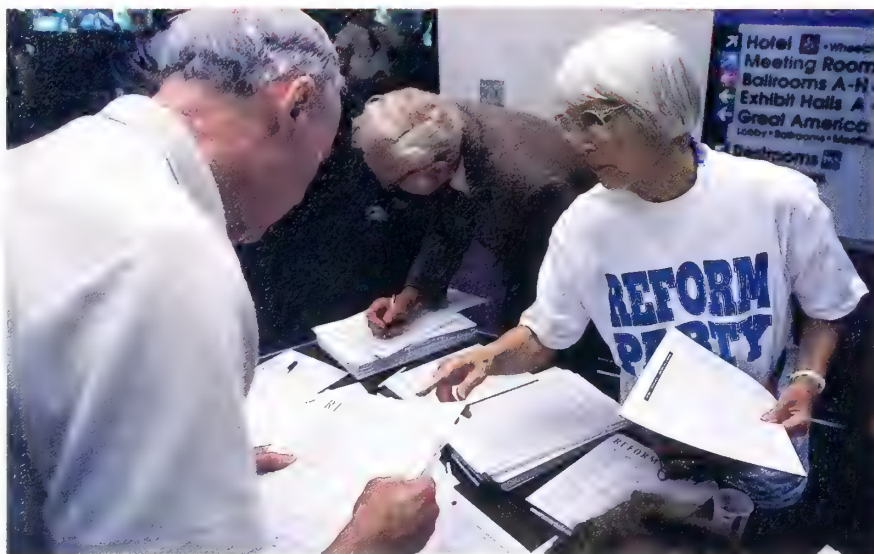
**NETWORKING** E-mail links for communicating with Kazarian, as well as for sending messages to be routed to institutional investors, the press, company managers and directors

**ANALYSIS** For selected investors, the lowdown on what Kazarian considers potentially hot investments, complete with sound clips

**RESEARCH** Surveys of employees at potential targets, information from rivals, intelligence on a company's products

**OTHER** Background on Japonica, Kazarian's investment company, plus job postings, Armenian online conferences, access to financial information, news clips





POLITICS

## MY CONTRACT CAN BEAT UP YOUR CONTRACT

Campaign pacts proliferate—but will the pledges be kept?

In the beginning, Newt created The Contract. And he saw that it was good politics. Now, Newt Gingrich's apostles—and even a few nonbelievers—are hoping to duplicate the political success of the House Republicans' 1994 Contract With America by devising their own campaign pacts. The Christian Coalition has one. So does Ross Perot's new Independence Party. After GOP candidates for Virginia's legislature unveiled their "Pledge for Honest Change," the state's Democrats responded with their own accord. And the folks who started it all are preparing to roll out a new version for 1996.

America's bout of contractmania may prove a passing fad. Yet some experts see the emergence of a new bond between politicians and voters: a written pledge makes it harder for officeholders to break campaign promises. Says GOP pollster Edward Goetas: "We're entering a phase where putting promises in writing—and then following through—is extremely important."

That's what Virginia's Republicans have concluded. GOP Governor George C. Allen hopes his party's pledge will

put the legislature in Republican hands this November for the first time since Reconstruction. Among the promises Republicans have made to win their seats: tougher prison sentences for juvenile criminals, work requirements for welfare recipients, and reduced taxes on business. "When we win, no one will be surprised when we keep our word," says Allen.

Virginia will provide a good test market of contract themes for congressional Republicans, who are already working on their '96 planks. Speaker Gingrich (R-Ga.) envisions a brand-new Contract that would include failed items from the first—term limits and a balanced-budget amendment—plus a flatter income tax.

And Democrats, who dismissed the Contract last year as a gimmick, are

**IT'S SIMPLE**  
The Perot party pledge includes calls for term limits, and campaign and lobbying reform

more eager now to play "Let's Make a Pledge." President Clinton is promoting an amorphous Middle Class Bill of Rights that includes tax cuts, college loans, and job training. Senator Bob Kerrey (D-Nebr.), chairman of the Democratic Senatorial Campaign

Committee, is drafting a contract to attract centrist Senate candidates to distance them from the party's liberal wing.

Among Kerrey's GOP-like priorities: a balanced budget, reforms of Social Security and Medicare, and stiffer penalties for criminals. The maverick moderate's goal is to change voters' perceptions of Democrats as tax-and-spenders. "The presumption is we're going to screw things up—and not without good reason," he admits.

**"SHAKE A TAMBOURINE."** Texas billionaire Perot is trying to build his Independence Party (called the Reform Party in California) by outlining a bipartisan contract that will include term limits and a balanced-budget amendment as well as issues ignored by Gingrich & Co.—campaign and lobbying reform. Perot wants to ban former government officials from lobbying for foreign interests, vows to "shake a tambourine in front of both parties" to see if they're serious about tough new ethics rules. "Hopefully, this will create an even better climate for us to deliver" on tough issues, Perot says.

The Christian Coalition, meanwhile, is pushing a "Contract with the American Family" that calls for tax breaks for families, school prayer, and government vouchers for use in both private and religious schools.

With the sudden proliferation of pledges, politicians risk overwhelming a fickle public. Or worse, politicians may renege on their contracts and make voters even more cynical. Says University of Indianapolis political scientist Stephen

Graham: "In the short term, I doubt whether the concept will be anything more than a marketing device." Even if that's true, contracts appear to be a very potent device: Increasingly, candidates are expected to hit the campaign trail without one.

By Richard S. Tedlow  
in Washington

### CONTRACTS GALORE

*First, there was the House GOP's Contract With America. Now comes a raft of imitators:*

**VIRGINIA** The GOP calls for work for welfare recipients, parental consent for teen abortions, tax cuts

**SENATE DEMOCRATS** Senator Bob Kerrey's plan would commit candidates to Medicare and Social Security reforms, lobbying restrictions, a balanced budget

**CHRISTIAN COALITION** Tax breaks for families with children, vouchers for private schools, a school prayer amendment

**ROSS PEROT** His United We Stand America is demanding a balanced-budget amendment, term limits, lobbying reform

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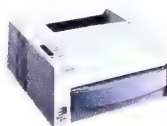


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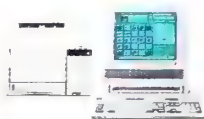
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**Canon**



## COMMENTARY

By Ron Stodghill II

### I'M MARCHING—IN SPITE OF FARRAKHAN

**O**n Oct. 16, the streets of Washington are expected to overflow with thousands of African American men participating in what has been dubbed the Million Man March. The event's goal: to promote unity among black men who are ready to take responsibility for themselves and their families.

Considering the dire social and economic conditions plaguing black communities, a pact among black men—if not women—to hold themselves accountable is long overdue. Sadly, though, the event has become embroiled in controversy. The reason: Its chief organizer is Nation of Islam leader Louis Farrakhan.

Not long ago, I decided to march. I realized the risk in this: Many of my white friends and colleagues would be puzzled, disappointed, even angered by my participation. Many would wonder what a 32-year-old, employed, college-educated black man could possibly have to protest. Even more, some would rightly question why I would parade behind a hate-monger such as Farrakhan. Unlike such leaders as Martin Luther King Jr., who spoke of building bridges between blacks and whites, Farrakhan spouts bigoted pronouncements that only deepen divisions between the races.

**SAD NUMBERS.** Those questions compel me to ask another: What other chance would I have to stand up in the U.S. with such a large group of black men—except in prison? A startling statistic: Almost one of three American black men in their 20s are behind bars, on probation, or on parole, says a recent study by the Sentencing Project, a prison reform group. One in 15 white men fall into the same categories. Each day, I encounter similarly discouraging studies on unemployment and dropout rates, or drug and alcohol addiction.



**BEHIND THE SCENES:** Women in a Chicago church help to organize the march

No doubt it is time for African Americans to change direction. Like the Congressional Black Caucus and several big church and community organizations—including the vaunted Southern Christian Leadership Conference and many local affiliates of the National Association for the Advancement of Colored People—my plan to march is based on a desire to respond to the deep crises facing all of us.

To me, this is not about race—although it may appear so on the surface. Sure, as a journalist I've listened in frustration over the years as my employers paid mostly lip service to the importance of bringing more blacks into largely white newsrooms. I've resented expectations that I should handle any "black story" that came along. And I've fumed when taxis wouldn't stop for me on city streets.

**LISTEN TO WOMEN**

**What other chance would I have to stand up with such a large group of black men—except in prison?**

But this march transcends such personal issues. It's about a collective change in mind-set required to prevent blacks from falling further behind other Americans. For years, we looked to the government to clean up our communities and patch up our families. Ultimately, though, we can blame only ourselves for what happens in our own backyards. Without discounting the need for some legislated solutions, the first crucial step is self-reliance. At such a crucial juncture, it is simply irresponsible to sit on our hands.

Farrakhan knows this. Few can deny him credit for developing a vision calling on "black men to stand unity to declare to the world that we are ready to shoulder our responsibility as heads of our families and leaders in our community." But the groundswell of support for the march hardly anoints Farrakhan as leader. "People are speaking for themselves," rather than for Farrakhan, says the Reverend James Demus, pastor of Park Manor Christian Church in Chicago, one of the march's organizers. Beyond his Nation of Islam bloc, trust in Farrakhan's ability doesn't reach as far as many whites believe. Indeed, although he would be loath to admit it—he did not respond to interview requests—Farrakhan has quickly become a minor actor in his own grand production.

Our most critical issues require solidarity in our race, not confrontation with others. As former Congressional Black Caucus Chairman Kweisi Mfume (D-Md.) told me: "This is a case where the message has become much bigger than the messenger." I only hope it stays that way.

*Stodghill is a Chicago-based correspondent for BUSINESS WEEK.*



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## DEALS

### THE ULTIMATE PHOTO OP?

Bill Gates has big plans for the Bettmann Archive

**S**omeday, perhaps, our PCs will turn into vast image banks. Students will cruise the Internet in search of archival photos to illustrate their term papers; lovers will seek out the perfect Toulouse-Lautrec painting to adorn their electronic greeting cards.

If that day ever comes to pass, there is an excellent chance that Bill Gates will make money from it. His Corbis Corp. owns electronic publishing rights to about about half a million paintings, prints, photos, and maps—the world's largest depository of digital images. And on Oct. 10, it announced the purchase of the Bettmann Archive, among the biggest collections of historical photos.

The acquisition will put more than 16 million images—from prehistoric cave drawings to the photo library of United Press International through 1990—in Gates's hands. Says Corbis Chief Executive Doug Rowan: "It's mondo. It's



**SNAP DECISION:** Bettmann's Gstalder and Corbis' Rowan

quite magical." It may even be profitable. Rowan, who wouldn't disclose the purchase price, says Corbis will digitize some 300,000 photos while the Bettmann, headed by longtime director Herbert Gstalder, continues operating its existing business in New York.

Gates, the well-photographed chairman of Microsoft Corp., founded Corbis in 1989, then calling it Interactive Home Systems Inc. Its mission: To acquire digital rights to fine art and photographic images that could be viewed electronically—on everything from computerized wall hangings to electronic books. Gates hopes its digital archive

will be used by publishing and advertising companies—by computer users who, for a fee, download images.

Though analysts say it has some licensing revenue, thus far, Corbis has licensed images to the Arts & Entertainment cable network for use in its videos and delivered fine art images to Midsoft for use in its Braveheart CD-

Experts say the dollar potential for electronic images could be huge. But they also say that in the traditional stock photo business, less than 1% of all images sell each year. Some question whether digital images have any more potential. "There's a lot of hype going on," says Don Barlow, a vice-president at The ImageBank.

Still, most traditional stock businesses, including The ImageBank, have been digitizing efforts under way. And the House of Representatives is spending \$5 million to digitize 5 million images. Gates, clearly, isn't the only believer.

*By Kathy Rebello in San Francisco*

## EXECUTIVE SUITE

### THE MANZI WHO KNEW TOO MUCH

His ideas weren't heeded, so Lotus' chief bolted Big Blue

**I**t was a shotgun courtship from the beginning. When Louis V. Gerstner Jr. made an unsolicited bid for Lotus Development Corp. last spring, he offered Lotus CEO Jim P. Manzi a job to help smooth the deal. To the surprise of many, Manzi warmed to the idea of a Lotus-IBM marriage. Maybe too much.

On Oct. 11, Manzi resigned his posts as Lotus CEO and IBM senior vice-president after it became clear that he would never win the larger role he had sought, people close to the executive say. Manzi had been lobbying Gerstner for weeks to adopt a plan that would combine much of IBM's sprawling software business with Lotus and give Manzi and his management team broad powers.

Manzi's proposal included some radical possibilities, sources close to IBM and

Lotus say. Among them: acquiring NEXT Computer Inc., the software company run by Apple co-founder Steven P. Jobs. "I have put my ideas on the table. I have been very straightforward about what my ideas are about how to run a successful software company," Manzi, 43, said when he announced his departure.

**FINE-TUNING.** If Gerstner has his own ideas for fixing IBM's stumbling software operations, he isn't sharing them just yet. The Lotus deal aside, he has done little but fine-tune.

IBM-Lotus teams have been working to mesh related products, but many operational issues remain. For one, sales and marketing are still handled separately. And Lotus executives gripe that IBM's hardware-driven sales force is hampering sales of Lotus Notes, the groupware program that Manzi describes as the "core asset in the arsenal of IBM's strategy now."

Gerstner will have to move quickly to



**OUTSPOKEN:** Manzi had some radical proposals

stabilize the situation. Landry, a Lotus senior vice-president and IBM network expert, and Robert Weiler, the senior president who runs Lotus, also were ready to go. They were setting off a scramble within IBM to change minds and head off an exodus. Another key Lotus executive, IBM doesn't want to be Notes creator Ray Ozzie. Those close to say he will stay to complete Notes 4.0, a major upgrade of the product due at yearend. After that, it's an open issue.

The big question: Who will run Lotus? Candidates include Michael D. Zisman, a key Lotus communications executive, and possibly Bruce Harreld, the former president of Boston Chicken Inc. recently hired as IBM's chief strategist. Even one IBM executive considers that replacing Manzi, an IBMer "would be the kiss of death. Your play, Lou."

*By Amy Cortese in New York City and Paul C. Judge in Boston*

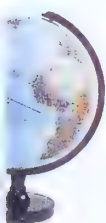


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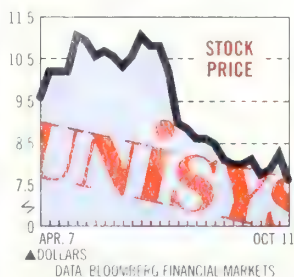
## NO CHEER FOR GIBSON GREETINGS

BANKERS TRUST MAY WELL have done wrong—but that won't get Gibson Greetings off the hook. The Securities & Exchange Commission on Oct. 11 settled its case against Gibson and two former executives, finding that the company failed to account properly for 1993 derivative transactions with Bankers. Gibson also failed to establish controls to track its positions, the SEC stated, and neither reported the associated risks nor kept books very well. In a lawsuit filed against Bankers and settled in 1994, Gibson Greetings claimed that the company lost at least \$23 million from the transactions.

## CLOSING BELL

### REBOOTING

Unisys wants to move out of mainframes into computer services. It won't happen too soon for Wall Street. The \$7.4 billion outfit's stock rose nearly 10%, to 8½, two days after CEO James Unruh disclosed plans on Oct. 6 to ditch a matrix management structure, cut costs by at least \$400 million by '96, and split operations. But by Oct. 11, investors had driven Unisys to 7%. After tumbling last year, revenues have been flat and first-half profits slipped 23%. Unruh's formula: "simplicity, not complexity."



## AN OLIVE BRANCH FROM JEROME YORK?

"I DON'T THINK A FOOD FIGHT in the press is in the best interests of shareholders," says Jerome York, Kirk Kerkorian's point man in his tussle with Chrysler. This after a combative Oct. 11 speech to bondholders in New York, in which York accused Chrysler Chairman Robert Eaton of unfairly "painting" Kerkorian as hostile, and flip-flopping on a pledge to invite large shareholders onto Chrysler's board. Still, York says, he would like to resume a "businesslike" dialogue with Eaton, perhaps later this month.

## CORESTATES WON'T CHANGE STATES

TERRENCE LARSEN, THE cautious and deliberate economist who runs CoreStates Financial, never really warmed to the idea of moving headquarters out of Philadelphia. So perhaps it was a good thing his deal to merge with Bank of Boston collapsed in July. Instead, CoreStates announced on Oct. 11 that it will pay some \$3 billion in stock for Meridian Bancorp, just outside town. But investors, unhappy with the deal's 24% premium clipped CoreStates stock by 3%—but sent it back up the next day.

## BOEING WORKERS TAKE A WALK

MACHINIST JOBS ARE SLIPPING away to Asia, and Boeing workers aren't happy about it. Some 32,000 employees walked off the job on Oct. 6 in what is likely to be a drawn-out dispute over the export of high-skilled union jobs. Boeing, like other plane makers, frequently transfers production over-

## HEADLINER: MICHAEL STEINHARDT

### A BIG PLAYER SIDELINES HIMSELF

Has Michael Steinhardt quit the hedge-funds business for good?

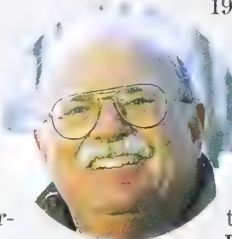
On Oct. 11, the 54-year-old investor announced plans to dismantle his \$2.6 billion financial empire and return most of his four funds' assets to investors by year-end. After two years of performance that has ranged from awful to merely mediocre, Steinhardt's portfolios in 1995 are up about 20% to 24%, net of fees and expenses, vs. 26% for the Standard & Poor's 500-stock index.

Steinhardt says that he will devote himself to two long-time passions—Demo-

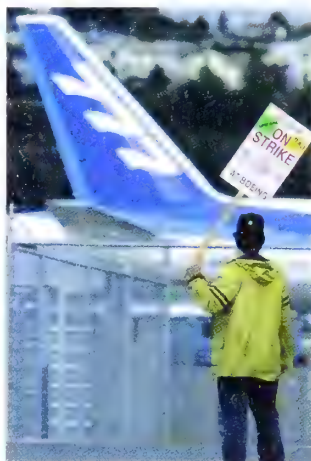
cratic politics and Judaism. But will that sustain him? Steinhardt took a year-long sabbatical in the 1970s and considered quitting last year, when his funds plummeted some 30% because of ill-fated currency and bond trading.

Even Steinhardt concedes that the decision to finally wind down his hedge funds is "irrevocable—but not irreversible." Indeed, he puts the odds of a return to the hedge-funds business at in 4. The smart money says the odds are even better than that.

By Gary Was



seas in exchange for governments' promises to purchase planes—and to keep costs down. The International Association of Machinists & Aerospace Workers, though, argues that the industry is nurturing future rivals by transferring technical know-how. Insiders say the walk-out could drag on for weeks.



**ANGRY RANK AND FILE:** Jobs are being exported to Asia

## FAKE FAT'S REAL DEBUT APPROACHES

WILL PROCTER & GAMBLE fat substitute, olestra, see the light of day? Eight days after P&G petitioned the Food & Drug Administration, it believes approval for its snacks may be nearing. It's to chip addicts are wailing. P&G says chips made with it would have no fat and few calories. Test marketing could begin in 1996.

## ET CETERA...

- American Airlines will flight attendants an average of 17% more over six years
- Healthsouth will buy Surgical Care Affiliates to create an outpatient surgery chain
- Netscape's bounty: \$0 to anyone who finds big bugs in its Navigator program
- Oprah lives! Winfrey promised she'd extend her talk show two more years



EDITED BY OWEN ULLMANN

## CONGRESS LOOKS READY TO REIN IN OUT-OF-CONTROL LAWSUITS

For Corporate America, overhauling the legal system to curb frivolous lawsuits and exorbitant damages has been a 16-year quest. And after the House and Senate passed widely differing reform bills, it looked as if 1995 would be the anniversary of failure. But leaders of the two chambers quietly nearing a compromise that could hand business a net victory over a powerful alliance of trial lawyers and consumer groups.

What's turned the tide? House Speaker Newt Gingrich (R-Miss.) has decided that it would be better to narrow differences with a less radical Senate measure than risk defeat for any plank in the GOP Contract With America. So, the House is expected to meet its demands for curbs on all civil suits, ranging from wrongful death suits to environmental damage claims. Instead, the Gingrich camp appears ready to settle closer to the Senate version, limiting only product liability disputes.

**FINING A DEAL.** Politicians are reacting to mounting public disgust with lawsuits as the Great BMW Coverup. In that case, Birmingham (Ala.) physician Ira Bolt won a \$2 million punitive award because the German auto maker failed to disclose that the fender of his new \$40,000 car had been repainted. "They have taken advantage of Dr. Bolt," Andrew W. Bolt II, the doctor's attorney, told jurors. Bolt of North America asked the Supreme Court on Oct. 11 to limit the damages. Under the emerging congressional pact, such payments would be a thing of the past.

Both lawmakers hope to cut a deal by Thanksgiving and pass a bill to President Clinton by yearend. They're betting voters' disillusionment with the legal system will prompt them to sign it. "Negative ratings for the justice system are worse than Bill Clinton's," notes Representative Christopher Cox (R-Calif.), a leading advocate of tort relief for busi-

ness. All these forces have prompted House Judiciary Committee Chairman Henry J. Hyde (R-Ill.) and Senate Commerce Committee Chairman Slade Gorton (R-Wash.), who are overseeing the legislation, to search for common ground.

Gingrich simplified their task by removing one contentious House provision absent from the Senate bill—setting limits on medical malpractice awards—and adding it to a Medicare reform bill. That paves the way for a deal. The compromise taking shape would shield defendants from huge damages in only certain types of lawsuits. They include manufacturers sued over defective products, businesses sued by

other companies, and so-called sympathetic targets, such as homeowners or nonprofit groups. Some plaintiffs—children in abuse cases or victims of discrimination, for example—would be exempted from damage limits.

That should be enough to please Corporate America, which cares most about curbs on product liability. Indeed, business, including groups once holding out for the House version, are ready to compromise. Reaching an agreement "is like cutting a diamond," says Victor E. Schwartz, a lobbyist for the probusiness Product Liability Coordinating Committee.

"If you hit too hard, it explodes into a million worthless pieces." Besides, business diehards expect the House to seek more restrictions in 1996.

All this unexpected talk of a deal has shocked tort reform opponents, who have been banking on a House-Senate stalemate. Now, they'll have to redouble their efforts. "It's going to be a battle royal," says Linda Lipsen, executive director of the Association of Trial Lawyers of America. But Congress seems to be in no mood for gridlock. That augurs well for a victory business thought it might never see.

*By Catherine Yang*



**LAWYER BOLT** and the \$2 million BMW

## CAPITAL WRAPUP

### SOUTHERN EXPOSURE

There's no Southern comfort for Democrats these days. Party stalwarts thought the worst was over on Oct. 9, when Senator Sam Nunn (D-Ga.) announced his retirement. But Representative Charles Wilson (D-Miss.), a flamboyant conservative who has fought rifles with Afghan rebels, will also leave after 24 years in the House. And sources say Representative Mike Parker (D-Miss.) will soon join three Magnolia State colleagues who have switched to the GOP.

### TRADE TWO-STEP

► As Commerce Under Secretary for International Trade, Jeffrey E. Garten scoffed at congressional schemes to merge U.S. trade operations into one agency. But now that he's leaving government to become dean of Yale University's School of Management, Garten has changed his tune. He favors combining the Export-Import Bank, Overseas Private Investment Corp., and Trade & Development Agency so that business can do one-stop shopping for global financing.

### DICK MORRIS' NEW MISSION

► How important has enigmatic Republican political consultant Dick Morris become to President Clinton? Important enough to help his new boss cut a budget deal with Hill Republicans. The publicity-shy Morris has been conducting quiet talks with Senate Majority Whip Trent Lott (R-Miss.)—whose 1988 Senate campaign he helped run—in hopes of forging a bipartisan accord. Other Clintonites are irked by the Connecticut-based consultant's rising influence.





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# THE DAIWA COVERUP WILL BACKFIRE ON THE BANKS

MOF's withholding of the facts enrages the U.S.—and damages credibility worldwide

**T**ime for a cleanup at Japan's mighty Ministry of Finance? The doyens of high finance at last week's International Monetary Fund and World Bank meetings in Washington had to wonder. As officials gathered to discuss how to further global financial cooperation and transparency, a six-week secret came to light. Word surfaced that at least one top MOF official had known about \$1.1 billion worth of losses due to fraudulent bond trading at Daiwa Bank Ltd.'s New York branch—without breathing a word to U.S. regulators.

The delay came as a slap in the face to U.S. Treasury officials. After a summer filled with trade dialogue and daily currency consultations between Tokyo and Washington, the communications breakdown was ironic at best and insulting at worst. After all, the U.S. played a big role in bringing down the super yen that has battered Japan's already weak economy. Top MOF officials such as Eisuke Sakakibara, deputy director general of the international finance bureau, had been in constant contact with U.S. Deputy Treasury Secretary Lawrence H. Summers to manage the yen-dollar exchange rate. But MOF's currency honchos claim that their banking colleagues down the hall kept them in the dark about the Daiwa mess. On the morning of Oct. 11, Finance Minister Masayoshi Takemura called Treasury Secretary Robert Rubin to say it wouldn't happen again.

The scandal makes a mockery of Japanese political leaders who promise a new spirit of cooperation. It is also likely to make the bad situation of the Japanese fi-

nancial system even worse. Instead of protecting the banks with its secrecy, MOF has further undermined their credibility at home and abroad. The punishment: Japanese banks, already paying a premium to borrow in international markets, could see their cost of capital rise further still. And domestically, mustering support for publicly funded bank bailouts won't be easy when coverups like Daiwa's are fresh in the minds of Japanese newspaper readers.

**EXPOSURE.** The world learned of this billion-dollar debacle on Sept. 26, when U.S. prosecutors charged a Daiwa trader with orchestrating an 11-year odys-

sey of financial fraud. MOF insists it didn't know of the fiasco until Sept. 13. Maybe not. Daiwa Bank President Akira Fujita says that as early as Aug. 1, he informed MOF's banking bureau chief Yoshimasa Nishimura, about a written confession from the New York trader explaining how he had racked up—the hidden—the billion-dollar loss. In fact, the letter had been sent on July 24.

Nishimura claims he did not want to bring the problem to U.S. regulatory attention until he got all the facts. According to a MOF spokesman, Nishimura told Fujita to determine Daiwa's exposure in a meeting attended

## MOF's One-Way Street

*Seeking help from Washington but clamming up over Daiwa*

**Apr. 19** Japan braces for a profit squeeze as the dollar dives to 79 yen. Meanwhile, the plunging Nikkei puts more pressure on the debt-laden financial system.

**May 16** After trade talks stall, Washington threatens to slap 100% tariffs on 13 Japanese luxury car models.

**June 23** The U.S. drops car sanctions as Japan agrees to targets for opening its auto market. The yen begins to fall.

**July 24** Toshihide Iguchi, head of Treasury bond trading for Daiwa Bank in New York, submits a written confession to his superiors in Osaka, detailing his effort to hide more than \$1 billion in trading losses over 11 years.

**Aug. 8** Daiwa officials inform Yoshimasa Nishimura, director general of MOF's banking bureau, about Iguchi's trading losses.

**Aug. 15** Coordinated dollar buying by the Japanese, U.S., and German central banks helps lift dollar to 98 yen, bringing relief to Japan's banks and companies. MOF and Treasury officials let it be known they are in daily contact.

**Sept. 18** MOF finally tells regulators in New York and Washington about Daiwa's trading fraud history.

**Sept. 22** New LDP President Ryutaro Hashimoto vows to cooperate closely with U.S. in turning around Japan's economy.

**Oct. 9** Daiwa President Akira Fujita and two other senior bank officials resign. U.S. Treasury officials incensed.

DATA: BUSINESS WEEK



king bureau associates. But he failed to give U.S. regulators, MOF's international finance crew, or even Takemura a heads-up. Says one senior MOF source: "He would have advised the banking bureau on the importance of sharing information with U.S. regulators." That kind of advice shouldn't be needed at the ministry. The lapse speaks volumes about the inner workings of this bureaucratic colossus, which rules over Japanese equivalents of the Treasury Dept. and Federal Deposit Insurance Corp. and works closely with the Bank of Japan. MOF also calls the shots on tax and budgetary matters. Financial policy is carried out in a clubby and opaque atmosphere, characterized by scant disclosure and cozy relations between regulators and financial executives. The system didn't seem to do any harm when everybody made a truckload of yen. But during the "bubble" maintaining a loose monetary policy akin to feeding steroids to an economy artificially pumped up by real estate stock speculation. The turbocharged Nikkei 225 stock average, commercial property prices, and Japan's five-year

## "If Daiwa was doing all this bad stuff, then how about the other guys?" says one high-ranking U.S. banker

run of 4.5% real growth rates came crashing to earth starting in 1990. Now, after four years of economic stagnation, the mandarins in the ministry's six-story fortress seem no closer to taking the needed measures to turn the economy around. In fact, MOF continues to cloak the dimensions of Japan's banking crisis, with estimates of nonperforming loans at less than half of the \$1 trillion figure many private analysts advance.

Coming on top of such dangerous understatements, the Daiwa cover-up further shakes international confidence in MOF's ability to cope. And Japan needs foreign cooperation badly. Even as ministry officials

were hiding the Daiwa loss, the U.S. Federal Reserve, Germany's Bundesbank, and the Bank of Japan were carrying out a behind-the-scenes plan to shore up Japan's financial system. Well-timed dollar-buying by central banks has driven the greenback up 26%, from its April low of 79 yen to around 100 now. The yen drop came as a huge relief to a Japanese economy on the verge of recession and caught in a deflationary spiral. It also helped Japanese stocks bounce back 24% from this year's low.

The Daiwa mess is likely to raise more questions about the true state of Japan's other banks. "If Daiwa was doing all this bad stuff, then how about the other guys?" says one high-ranking U.S. banker. Instead, investigation of the Daiwa fraud is sure to widen. Even before the scandal broke, House Banking Committee Chairman James A. Leach (R-Iowa) was calling for congressional hearings into Japan's banking crisis. And back at home, the Japanese Diet will begin examining the Daiwa affair in the next several weeks.

**CUSHY JOBS.** Before the scandal broke, MOF had proposed tougher disclosure requirements for Japan's lenders.

But the Daiwa case suggests the Ministry is still far from demanding the kind of managerial accountability necessary to make any reforms stick. For instance, while Daiwa's Fujita resigned on Oct. 9, he will stay with the bank as a paid adviser—and so far, MOF isn't objecting. One reason is that MOF has little incentive to be tough with the banks it supervises, which traditionally offer paid sinecures to retiring ministry officials in a practice known as *amakudari*, or "descent from heaven."

Still, MOF is sure to find out that withholding vital information from international investors and regulators isn't cost-free. Already, the U.S. is taking steps to limit federally backed American lenders' exposure in Japan. Treasury and Federal Reserve officials say that despite their anger at the Daiwa affair, cooperation on international trade and currency issues will continue. But even if it does, the markets are likely to show their displeasure by making it still harder for the beleaguered Japanese banks to raise money. MOF will have only itself to blame.

By Brian Bremner in Tokyo, with Dean Foust and William Glasgall in Washington







INDIA

## GET THE 'FOREIGN DEVILS'

India's backlash against multinationals gains strength

**T**he three-story Kentucky Fried Chicken restaurant in downtown Bangalore looks like any other fast-food outlet, with one notable difference: A handful of armed police officers stand guard outside the glass doors, and 30 more wait in a beat-up red bus parked nearby.

The cops are needed because the Karnataka Farmers Assn. has threatened to destroy the new restaurant and toss the company out of India. The association says the fast-food chain favors big farmers and hurts small ones. It also argues that KFC's chicken is carcinogenic: too much monosodium glutamate. Not surprisingly, the controversy has hurt KFC's business. "When you've got armed guards outside," says Sandeep Kohli, managing director of PepsiCo Inc. restaurants for South Asia, "it scares people away."

American companies find they are not quite so welcome in India as Prime Minister P. V. Narasimha Rao's government once led them to believe. The rhetoric is



**ROUGH TREATMENT:** India's xenophobia—rooted in its colonial past—has led to demonstrations aimed at Pepsi and its Kentucky Fried Chicken units.

getting much hotter: Politicians in opposition parties rail against the "foreign devil" and call for demonstrations against Pepsi and Coca-Cola, in which bottles of the beverages are smashed.

**FRINGE GRUMBLING.** It's troubling, too, that foreigners get so little public support from their supposed friends in India. Rao's weak and divided Congress Party (I), which once pushed economic reforms, now seems to be letting them drift along. These Congress leaders dismiss protests against foreign companies as the grumbings of fringe groups.

But events of the past few months show they cannot be ignored. DuPont Co., forced out of one Indian state because of concerns over hazardous chem-

icals, is facing similar opposition to a new one. Mahatma Gandhi's grandson has filed criminal charges against a TV network owner Rupert Murdoch, insulting his grandfather. Several projects also are under attack. The most notable example of repudiation, of course, was Enron Corp.'s \$2.8 billion installation project in the state of Maharashtra. Negotiations are resuming, but opposition will still be tough.

Most of the challenges have been against American companies, which bear the brunt of Indian worries about cultural imperialism. Japanese and German companies, in contrast, encounter few such problems. Increasingly, the criticism is directed against not only



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consumer goods but also more sophisticated products and services. Telephone company U S West Inc., for example, is facing opposition in southern India. It won a bid to create a pilot telecom project based in Tamil Nadu, but now critics are charging it benefited from government favoritism. "Companies should be very worried about this," warns Dilip Cherian, who advises KFC, DuPont, and U S West. "This is not a trend that will stop today."

None of this is very good news for India's four-year-old program of economic liberalization. The danger isn't so much that the reforms will be actively dismantled but that they might simply erode—a casualty of India's unrelenting political polemic. Although many major U.S. companies are determined to stick it out in the world's second-most-populous nation, others may decide to stay away. U.S. direct investment stood at a mere \$318 million at the end of 1994, according to the U.S. Commerce Dept.

The widespread anti-foreign feeling in India has deep roots. The legacy of Britain's East India Co. has bred a suspicion of foreigners that applies to companies, ideas, even tourists. "It is there. You cannot discount it. You cannot ignore it," says Jay Dubashi, economic adviser to the Bharatiya Janata Party (BJP), which preaches what it calls "economic nationalism."

**SHORT FUSE.** What the public thinks matters. India is the world's largest democracy. And many say it's a hyperactive one, where people are quick to protest. "India's problem is that it has an overdeveloped democracy and an underdeveloped economy," says one government official. With one-third of the country's 900 million people living below the poverty line, it's not hard for politicians to rile the poor.

What foreign companies are discovering is that India's middle class also feels uneasy about multinationals swooping down to feed, clothe, and entertain them. They may buy Kellogg's cereal, Levi's jeans, and Sony TVs because they like the quality, says Titoo Ahluwalia,

chairman of Marketing & Research Group Ltd. in Bombay. But, he says, "the average Indian has two sides to him. There's one side that's a consumer and the other that's a voter." A recent poll conducted by *The Times of India* in the country's largest cities showed that more than half the respondents were against KFC and any other foreign investment that does not bring in technology. Most Indians have "a raw nationalist nerve," says Dubashi. "It needs events to bring it out."



## FEARFUL One surprise: The reluctance of Prime Minister Rao's government to defend multinationals. Why? His Congress Party faces a tough election

One event was the controversy over Rupert Murdoch's Asia-wide Star TV satellite network. In May, a guest on a Star talk show, *Nikki Tonight*, called Gandhi a "bastard." The network bowed to public pressure and canceled the show. But now Tushar Gandhi, grandson of India's most honored figure, has filed charges against Murdoch of libel and criminal defamation.

Such incidents provide propaganda fodder for Indian industry, which is fearful of foreign competition. The Star TV debacle provided ammunition for media companies trying to keep out overseas rivals. The incident also prompted calls to crack down on satellite networks—something much more difficult to do, since their signals come from outside the country.

The BJP took that kind of popular opinion into account when it and its coalition partner in Maharashtra, the Shiv

Sena, went after Enron. The ultranationalist Rashtriya Swayam Sevak party had already stoked up local resentment against the Houston company.

**"NOT POTATO CHIPS."** The Hindu right seems divided over just what kind of foreign investment should be allowed. The BJP has adopted a much less phrase—"microchips, not potato chips"—to describe what sort of investment India needs and what sort it doesn't. It seems to hold out the prospect of technology-related investments v

move forward. But other voices seem eager to stall most investment. "I'm not saying I don't want multinationals at all," says Swaminathan Gurumurthy, head of the Swadeshi Jagat Manch, another violently nationalist party. "But having all of them entering the country at the same time may be good."

One surprise has been the refusal of the Indian government to defend companies, such as Enron, that it helps lure in. The reason is that the Congress Party must compete in national elections early next year and faces stiff competition from the BJP, which doesn't want to alienate voters by seeming proforeign. The party has even tried to move in a quieter way, so of the opposition's

tionalistic moves. Shortly after the government of Maharashtra changed the name of the state capital from Bombay to the original pre-British name Mumbai, the Congress Party renamed Connaught Place, New Delhi's business district, after Indira and Rajiv Gandhi.

Foreign executives acknowledge India's debate over how and when to them in is valid. But they are concerned about its tone. "Economic nationalism straddles the line between rational economic debate and xenophobia," says Davis, project director of AES Transporter, whose power project in the state of Orissa has run into trouble from a state government. How India walks the line between rationality and xenophobia could determine its ability to attract investment dollars and, ultimately, stimulate prospects for economic growth.

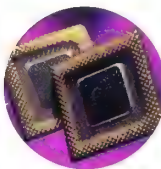
By Sharon Moshavi in New Delhi



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## CHINA

### WINDING UP FOR THE BIG PITCH

Advertising mushrooms in China, despite Beijing's heavy hand

**W**hen China adopted a tough new advertising law earlier this year, even the supposedly unstoppable drumming bunny in the Duracell battery commercials came to a halt. The government ordered the ad off the air because the bunny endurance contest broke new rules that ban superlative

prize: an ad market that has quadrupled, to \$3 billion, over the past three years and is expected to soar to \$22 billion by 2000—compared with \$55 billion in the U.S. last year.

A lot of the growth is fueled by multinationals vying to win the minds and wallets of China's expanding middle class.



**OUTDOOR OUTBURST:** Billboards are blossoming—but cigarette ads are banned

claims and comparative advertising. For Ogilvy & Mather Advertising's Beijing office, which handles the American battery company's China ad account, it was back to the drawing board.

The new regulations are just one of many challenges facing ad agencies and their clients as they jump into what promises to become one of the world's largest advertising markets. They are confronting an uncertain regulatory market, open discrimination against foreign advertisers, and difficulty in doing business with media that are still closely controlled by the government.

**WINNING MINDS.** But encouraged by the rising multinational presence in China and the fast growth in ad spending (chart), the rush is on. In addition to 43,000 local ad shops scattered across China, there are now 167 foreign joint ventures, all with local partners. The

There are now more than 300 million households in China that have bank savings, which total \$175 billion. And consumers are eager to buy goods, with their spending predicted to more than double, to \$743 billion, by 2003.

Still, advertisers have to keep an eye on the government, which is moving swiftly to regulate an industry often

considered chaotic. Just a year ago, it abounded for everything from toothpaste said to fend off senility to face soaps to wash away wrinkles. The law adopted on Feb. 1 was designed to curb in the most extravagant product claims but has created big problems for foreigners. "Everyone looked to the ad as a savior coming in on a big white horse. It's been anything but," says Mary Peng, executive director of DDB Needham, Young & Rubicam, China.

**INNER CIRCLE.** To make sure ads met the guidelines, Beijing holds everyone—agency, client, and media—responsible for infractions. The new curbs prompt agencies to redo more than 100 ads in Beijing alone. When DDB Needham geared up to introduce Budweiser in China, the agency quickly discovered that saying "King of Beers" wasn't acceptable. Likewise, when the agency wanted to tell the Chinese that the beer was America's favorite, they had to come up with statistics proving it.

Another headache for foreign agencies is China's discriminatory pricing policies. Some Chinese media vehicles charge imported brands up to 10 times as much as local brands pay for ad spots. Discrimination is unlikely to end until China is accepted into the World Trade Organization, which prohibits such practices.

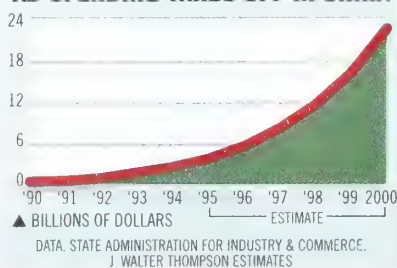
Meantime, with demand for space high, arbitrary decisions to replace ads with special programs or articles are common. Advertisers are required to pay 100% of fees in advance—and usually a struggle to recover the costs if the ads don't run.

The growing market for outdoor advertising has also proved challenging. With locations multiplying everywhere—from bus-stop kiosks, telephone booths, and shop awnings to expensive electronic display signs—the government has recently imposed new controls. Cigarette advertising, already banned from television, radio, and print media, is finding its once-reliant billboards disappearing. In August, Guangzhou joined Beijing in banning outdoor cigarette advertising, a move that hit tobacco companies and agencies hard.

Faced with all these headaches, few if any—foreign agencies are turn of profit. Most say optimistically that it will be at least two years before they are in the black. But given China's potential, that's not too long to wait. More problems bound to pop up in China, ad agencies will have to outlast more than just the Duracell bunny.

*By Dexter Roberts in Beijing*

#### AD SPENDING TAKES OFF IN CHINA







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## LONDON CALLING

Sources say Reichmann's single-minded pursuit of the huge project allowed him to beat the odds

## BRITAIN

# THE REICHMANN RECONQUEST

How the developer and friends won back Canary Wharf

It was close to midnight in London on Oct. 2 when 13 banks issued a three-sentence press release saying they had just agreed to sell Canary Wharf Ltd., Europe's biggest real estate development, to a small group of investors for \$1.2 billion. For the banks, it was the end of a troubled stint as Canary Wharf's owners. But across the Atlantic, it was the final chapter of a long crusade by Toronto developer Paul Reichmann to win back the project he had lost and prove his vision was right.

When the fax confirming the deal arrived, Reichmann simply leaned back in his chair and smiled. His doggedness had paid off spectacularly. He and the other new owners—the Tisch family, fund manager Michael F. Price, banker Edmond Safra, and Saudi Prince Alwaleed bin Talal bin Abdulaziz Al Saud—have ambitious plans to put more office buildings and a luxury hotel on the property, which already has 4 million square feet of developed space. One close friend says Reichmann's coup, which gives him just 5% of the project, has rejuvenated the 65-year-old. "Anyone else would've thrown in the towel," says the friend. "Not Paul. He's like a young man just starting out."

Reichmann's chase began shortly after May, 1992, when Canary Wharf,

caught in London's office glut, defaulted on \$900 million in loans. Canary Wharf's collapse helped push Reichmann's entire real estate company, Olympia & York Developments Ltd., into bankruptcy. Reichmann swore to friends he would get the riverside development back. "It never left his consciousness," says one banker who meets regularly with Reichmann.

Just four months after the bankruptcy, Reichmann mounted a \$500 million bid for the project with backing from New York financiers Sanford I. Weill, Lewis S. Ranieri, and the Tisch family. The banks, which ended up with Canary Wharf after O&Y defaulted, turned him down. "They thought he failed as a steward, and they weren't about to sell it back to him at a discount," recalls one banker.

**THATCHER'S BREAKS.** A year later, in October, 1993, Canary Wharf emerged from bankruptcy. With the project attracting more high-quality tenants, Reichmann put together another bid, for \$700 million, with the Tisch brothers as well as Republic National Bank of New York's Safra and Mutual Series fund manager Price. Reichmann also learned that Prince Alwaleed was putting out feelers. Reichmann visited the Saudi royal on his yacht off Cannes in

August, 1994, and tried to recruit him to his side.

Yet the prince persisted in his bid, which the banks ultimately rejected. Another offer emerged suddenly from New York developer Jerry Speyer. Alwaleed says he and Speyer briefly discussed an alliance. Reichmann resumed his courtship of the prince, this time successfully. "Reichmann knows how to manage real estate better than anyone else in the world," the prince says.

With solid backing in place, Reichmann submitted the winning bid of \$1.2 billion. Reichmann priced his bid low because he figures tax breaks bestowed by the Thatcher government on Canary Wharf can help him. His intention, says a source, is to sell some of the buildings to British companies with large tax shelters. The buyers get to reduce their taxes by using the tax shelters, and Reichmann gets back the space. The sale proceeds will repay a \$260 million bridge loan Reichmann is obtaining from grain company Cargill Inc. to round out his financing.

Some of the rejected bidders think history could repeat itself if Reichmann starts building again using leverage. "So, says Price, who thinks the site can easily handle new construction. "Fourteen buildings are built, the plans are done, the tax benefits are there, and people are building large buildings," he says. Alwaleed is no secret of his desire to build a Seasons hotel on part of the undeveloped acreage. Even without the aid of "we are looking at rates of return in excess of 20% right from the start," says. And Paul Reichmann is looking for a comeback as one of the world's real estate magnates.

By Paula Dwyer in London, and John Rossant in Rome



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EDITED BY ROSE BRADY

## ROBERT RUBIN'S UPHILL FIGHT OR NO MORE MEXICOS

The months it took to cobble a global bailout together after the Mexican peso crashed last winter left no one satisfied. That has prompted Treasury Secretary Robert E. Rubin to ask if there's a better way of dealing with crisis-style crises. His answer: a \$52 billion superfund devoted to meet financial panics before they spread around the world. Says Rubin: "Our response mechanism must be as fast as the markets."

It's an ambitious idea—maybe too ambitious. Rubin's plan is backing from major industrial economies during October's annual meetings of the International Monetary Fund and World Bank. But the finance ministers, and many bankers and key managers, think the IMF and emerging-market countries should focus more on prevention than relief.

Across the developing world, these critics argue, countries need to shore up domestic savings, speed privatizations, and repair weak financial systems to immunize themselves against the ebb and flow of global hot money. They must radically improve the quantity and quality of information available to investors. Only by taking these steps, critics maintain, will investors and policymakers be able to spot signs of trouble before they mushroom—take actions to forestall another collapse. As Bank of Tokyo Chairman Toyoo Gyohji says, "It's vital that we have a market-based approach to diagnosing and managing crises."

**FRIENDS.** A key part of avoidance will be greater surveillance of the developing world. Angered by Mexico's unwillingness to release data on its sinking foreign exchange reserves in the runup to 1994's devaluation, the IMF is insisting that aid recipients provide more information than ever, including data on savings, trade, currency holdings, and global debt. Other Washington agencies are also working to improve the

developing world's information flow. The World Bank's International Finance Corp., for example, will soon start releasing daily updates on trading on 27 emerging bourses. It has also teamed up with IBCA Ltd., a London credit-rating agency, to set up local rating organizations across the Arab world. And the World Bank is providing policymakers with software packages that lay out the impact of devaluations, tax rates, and privatization schemes on their economies.

Even with such efforts, some emergency aid probably is still in order. But can Rubin raise \$52 billion? His superfund would double the \$26 billion in credit lines the U.S. and its industrial allies already have for emergency financial assistance through the IMF. The Treasury chief is counting on Washington's wealthiest allies, especially such Pacific Rim nations as Malaysia, South Korea, and Australia, to provide much of the additional cash. But many are cool to the idea. Some bankers feel Asians will agree to ante up funds only when their own markets get hit by a crisis far away. And across the region, finance ministers are demanding a say in how their contributions are spent—something industrial countries are not yet ready to grant.

Many industrial countries also may be reluctant to back their approval with money. Germany, facing budget constraints, is wary of the superfund plan, and U.S. Republicans, who were critical of the Mexican rescue, will surely scrutinize new efforts. "Congress and parliaments everywhere are getting stingy," says Hung Q. Tran, head of equities for Deutsche Morgan Grenfell in Singapore. "The crux of the matter is money."

If Rubin and his allies stress reform and prevention enough, perhaps his superfund won't be needed. But given the hurdles it faces, the fund may not be ready for prime time anyway.

*By William Glasgall, with Dean Foust and Bill Javetski, in Washington*



**RUBIN:** Too little backing?

## GLOBAL WRAPUP

### MAKING DAIMLER

Daimler Benz Chief Executive Officer Jürgen E. Schrempp is moving quickly to knock the loss-making industrial group into shape. On Oct. 10, Schrempp inked a deal to sell subsidiary AEG's low-voltage transmission division to General Electric Co. The next day, European Union antitrust regulators said they expect to allow Daimler Benz to merge AEG's train-making activities into a joint venture with ABB Asea Brown Boveri (ABB) Ltd.

The price General Electric paid for the AEG unit, which had 1994 sales of \$225 million, was not disclosed, but brokers in Frankfurt guessed it was \$70 million or less. AEG, which expects to lose more than \$420 million this year, has already divested its white goods, lighting, and electric metering businesses. Schrempp is now likely to merge AEG's diesel engine and microelectronics divisions into the Daimler empire. Then he can attack his company's biggest problem: troubled Daimler Benz Aerospace (DASA).

### MEXICAN PENSION REFORM

► Mexico is facing mounting pressure from the International Monetary Fund, World Bank, and international investors to create privately managed pension funds to pump more savings into the economy. Finance Secretary Guillermo Ortiz is already working on proposals to reform Mexico's social security system. Foreign banks with extensive operations in Mexico, including Citibank, are studying the possibility of offering privately managed pension funds if Ortiz' scheme moves forward.



# CURE? WELL . . . PROFIT? SURE

Herbal sales will top \$2 billion in '95

**C**ould coming on? Forget the Contac. Zip right on by the Tylenol Cold. A new breed of marketer sharing shelf space with those national brands is hoping you'll pick up some echinacea. Or maybe a packet of little brown pills packed with ground-up willow bark, ginger root, and herbaphedia. Or even the homeopathic onion extract that, oddly enough, is supposed to help keep tears away.

Once strictly counterculture, such exotic—and sometimes questionable—remedies are going mainstream. Drug-store chains ranging from Eckerd Corp. to Osco offer herbal potions and pills as well as other alternative medicines. "It's incremental sales and it's profitable," says Dale Rogers, senior merchandise manager at Drug Emporium Inc., a 212-store chain. Makers of ginseng advertise the herbal cure-all everywhere from TV's *Wheel of Fortune* to drive-time radio shows—even though it has never been proven to cure anything. The Internet brims with catalogs of such alleged herbal cancer-fighters as schizandra berries and cat's claw.

**ACTIVE ROLE.** For retailers and manufacturers, this is getting to be one healthy business. Herbal-remedy sales alone are growing at double-digit rates and should top \$2 billion at retail this year, says the American Botanical Council. Homeopathic drug sales are likely to top \$200 million. Big players such as Nature's Bounty Inc. in Bohemia, N. Y., can barely keep up with demand. The company's sales have more than doubled since 1990, to \$156.1 million last year, while net income has grown tenfold,

to \$7.8 million. "People are taking a far more active role in their health and well-being," says James P. Flaherty, the company's marketing vice-president. "We're going to be as aggressive as we can be."

But are these New Age nostrums good for what ails you? Plenty of experts are skeptical. "An awful lot of it is snake oil, pure quackery," contends Dr. John H. Renner, a family physician in Independence, Mo., and an official with the National Council Against Health Fraud, a consumer-advocacy group. Indeed, some alternative remedies have proved harmful, even fatal.



Just because a substance is natural doesn't mean it's safe. After logging more than 100 complaints of side effects ranging from dizziness to heart attacks, and even a few deaths, the Food & Drug Administration in February issued a warning against Nature's Nutrition Formula One, a line of energy boosters. The problem stemmed from the interaction between the herb (known chemically as the amphetamine-like ephedrine), a staple of many alternative remedies, and caffeine-containing kola nuts. The manufacturer, Tensar-based Alliance U.S.A., has since dropped the kola nut. And just because a remedy is on a major retailer's shelf doesn't mean a warning, either. Traditional drugs marketed for specific health problems are subject to intense scrutiny by the FDA.

Not so dietary supplements; rules governing them were liberalized last year.

As long as makers of such supplements do promise a cure for a specific ailment, they don't have to prove much of anything. For the most part, the FDA's authority extends only to claims made on the label, while the Federal Trade Commission is responsible for claims made in sales brochures or ads.

Some manufacturers are proving adept at suggesting much without promising anything. They can't say feverfew alleviates headaches, but can say it helps "normalize blood vessel tone." They can't claim echinacea cures colds but claiming it promotes well-being during the cold season is acceptable. "We're learning to search the thesaurus," says Derek H. Hall, chief executive of \$100 million-a-year Nature's Way in Springville, Utah. "I can't use the word 'cure' or 'prevent.' I can use 'maintains.'"

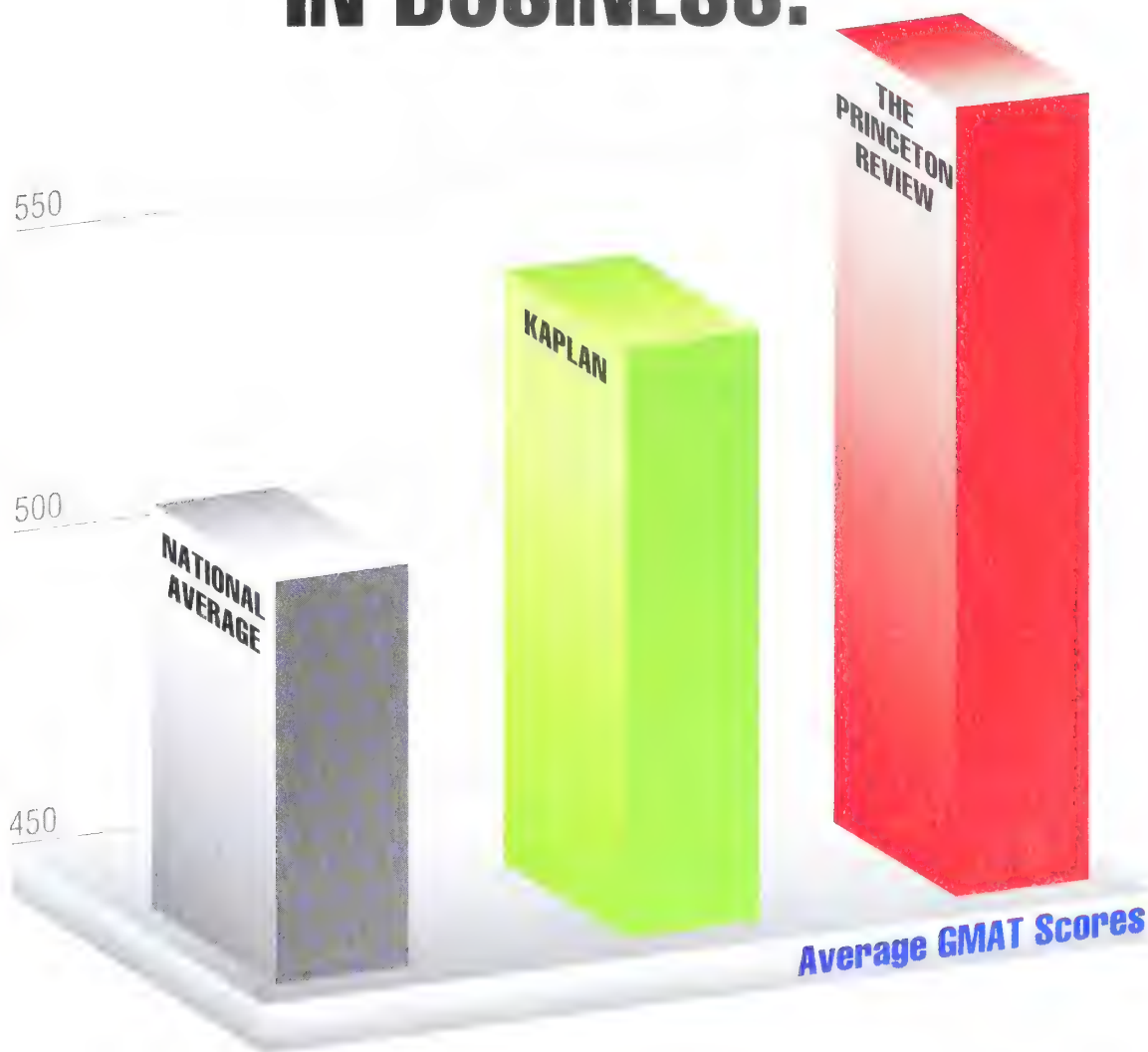
The difference in the claims made can be

## Take Two Dong Quais and Call Me in the Morning

| HERB      | USE                                        | COMMENTS                                                                                                      |
|-----------|--------------------------------------------|---------------------------------------------------------------------------------------------------------------|
| COMFREY   | Wound healer, antiulcerant, blood purifier | Widely sold. May cause liver damage when taken internally; linked to at least one fatality. Banned in Canada. |
| DONG QUAI | Various gynecological complaints           | Popular Chinese plant. Hasn't been shown to be effective.                                                     |
| MA HUANG  | Nasal congestion                           | Effective, but can raise blood pressure and speed up the heart.                                               |
| FEVERFEW  | Migraine, arthritis                        | Lacks long-term toxicity tests to determine safety.                                                           |
| GINSENG   | Aphrodisiac, anemia fighter                | No proven efficacy for humans.                                                                                |
| YUCCA     | Arthritis                                  | Probably harmless, but hasn't been proven effective.                                                          |

DATA: THE HONEST HERBAL, VARRIO E. TYLER, PURDUE UNIVERSITY

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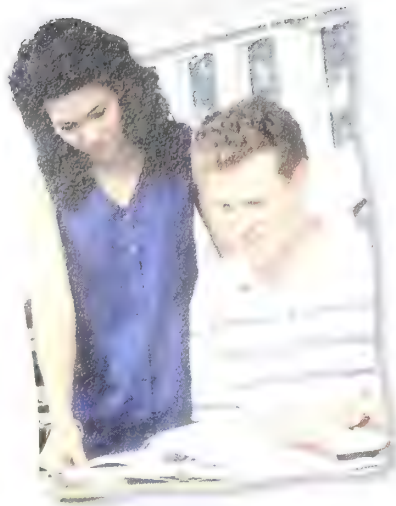
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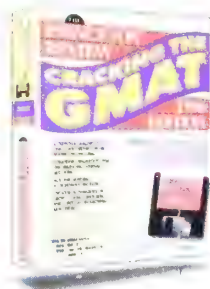
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—but the difference in what's behind these claims is enormous. Merck, Sanofi-Schering, and Bristol-Myers Squibb, for example, have spent hundreds of millions of dollars developing and testing cholesterol-lowering drugs for patients battling heart disease. But some herb companies make similar claims for garlic with much thinner research. Pharmavite Corp. says its Nature Made brand garlic helps reduce cholesterol, though it warns that the product isn't intended to diagnose, treat, cure, or prevent any disease.

Even such vague claims rile some lawyers. Bruce A. Silverglade, legal affairs director for the Washington-based Center for Science in the Public Interest, says the new claims are "dangerously close to disease-prevention promises." He says herb companies ought to be subject to the same rigorous science as the makers of Tylenol or Advil.

**WONDER?** Regulators from state attorneys general to the FTC are stepping up their scrutiny of alternative-medicine marketers. Last year, mall retailer General Nutrition Inc. agreed to pay a record \$2.4 million to settle charges it violated prior disciplinary orders.

Pittsburgh company, which didn't admit fault, was accused of failing to substantiate disease-treatment, weight-loss, and muscle-building claims on more than 40 products. In August, the Minnesota Attorney General sued marketer Carolyn McClendon for deceptive trade practices after she hawked a treatment for everything from AIDS to cancer to eczema on CompuServe. The wonder drug, germanium, a mineral linked to at least six deaths and permanent kidney damage. McClendon withdrew the electronic pitch without admitting guilt.

Of course, some herbs are effective. Aspirin, after all, was originally derived from willow bark. And a potent cancer fighter, Taxol, was initially made from the bark of yew trees. Chemists say that pure synthetic versions work better. But no matter what the scientists say, plenty of consumers will snap up alternative medicines. "If at all possible, I don't put anything into this body that is not natural," says Miami management consultant Dragana Carolyn Kvajnic. "I try to stay away from antibiotics. I try to stay away from Tylenol."

But be sure, conventional remedies don't always work so well, either. Anybody who's ever been made drowsy by a decongestant is a testament to chemistry's shortcomings. Some would-be buyers of the alternative might want to recall the old saw about cold treatments: Take the pill and the cold will go away in seven days. Don't, and the cold will hang around for a week.

By Joseph Weber in Philadelphia, and Sandra Dallas in Springville, Utah

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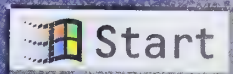
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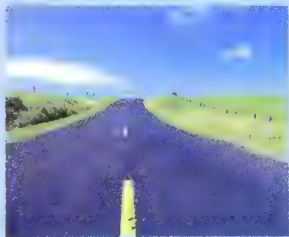
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# VIRTUAL B-SCHOOLS

## Beaming classes to companies from Daewoo to Disney

**A**fter a long, frenetic day at work, weary managers file into yet another corporate conference room. They sit and stare at the video-screen image of a business school professor who is hundreds or thousands of miles away. The teacher can't see the students. If they want to ask a question, they must first push a button on a small numeric keypad in front of them.

The executive classroom of the future? Maybe. Harvard business school has beamed some of its professorial stars, such as strategy guru Michael Porter, into alumni clubs around the world. The University of Michigan offers customized MBA degrees via videoconferencing to managers at Daewoo Corp. in Korea and Cathay Pacific Airways Ltd. in Hong Kong. Sloan School Dean Glen L. Urban is making "long-distance learning" a key priority, while Dean Paul Danos at Dartmouth College's Amos Tuck School plans to use satellite-video classrooms to more effectively bring the outside business world onto his isolated Hanover (N. H.) campus.

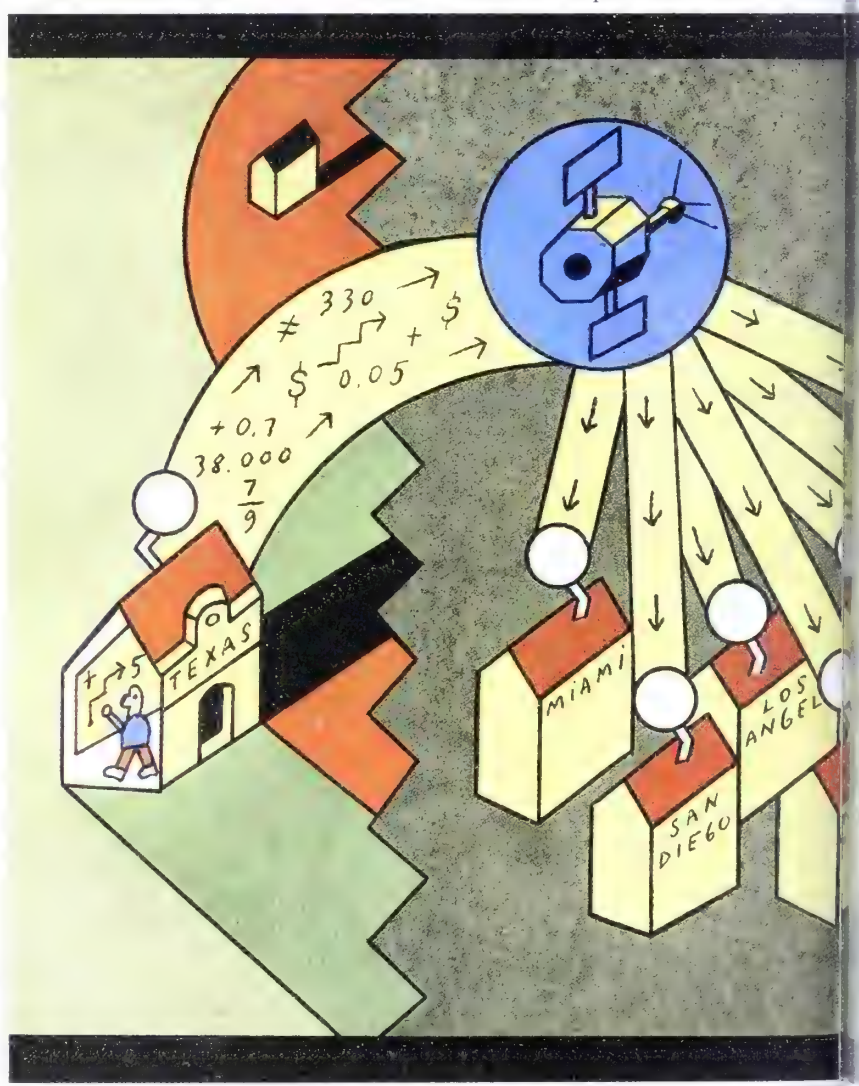
**CUSTOM COURSES.** Suddenly, almost everybody in the world of executive education is talking about long-distance learning. Business schools see it as a way to better spread their resources and for their faculty to have more impact. "The new techniques and technologies of distance learning hold the potential to revolutionize executive education," says Alan F. White, senior associate dean at the Massachusetts Institute of Technology's Sloan School of Management.

Long-distance learning is one more facet of a trend that has been reshaping the world of executive education for years: the relentless drive to make mid-career instruction more practical, meaningful, and efficient. Companies continue to demand that executive education achieve specific, real-world goals and immediate payoffs. More B-schools and companies are collaborating to create custom courses, with content designed

specifically for the employees of a single company. Increasingly, business schools are ditching long multiweek programs in favor of shorter courses to fit the time constraints of harried managers. After a 38-year run, MIT's Sloan School last year canceled its eight-week Program for Senior Executives because it could not get enough participants to enroll in it.

But it's the satellite classroom that is

drawing the most attention. So far, the most ambitious effort at high-tech executive education is being mustered by Westcott Communications Inc. and eight business schools ranging from Babson College to the University of Pennsylvania's Wharton School. The venture, Executive Education Network, already boasts nearly 100 corporate classrooms at such companies as Eastman Kodak





alt Disney, Texas Instruments, and Oracle Technology. "I think this can be very big," says Jack T. Smith, president of Westcott, an education and training company based in Carrollton, Texas. "Building this to 500 corporate sites is not out of reach."

Why would anyone seriously interested in business education want to gaze at a TV tube? Corporate America's long starvation diet has led to the feeding of tens of thousands of managers. Few companies can now afford to send the survivors to weeks or months of off-site executive education courses. One chief executive puts it: "If we do without someone for a week, we probably do without them for good."

**HT SCHOOL.** Yet with vast changes in the landscape of business, many managers find themselves lacking the skills and knowledge to tackle new and more demanding responsibilities on the job. They may not have time for education anymore, the thinking goes, they need it more than ever.

So more companies and business schools are exploring the possibility of

## Few companies can afford to lose the survivors of downsizing to weeks or months of off-site executive education courses

offering managers live, interactive classes delivered via satellite to corporate sites—often after work hours. The University of Michigan's business school is working with a consortium of companies headed by British Telecom to deliver live video courses next spring in the U.S., Europe, and Asia. At Westcott, dozens of B-school professors, working with an Emmy-winning producer, are putting on makeup and polishing their classroom lectures for TV delivery.

Such ventures also give business schools the opportunity to experiment with technology—and broaden their revenue streams. "Is this a moneymaking venture?" asks Robert E. Mittelstaedt Jr., vice-dean of executive education at

Wharton. "Absolutely. But it's also an experiment in how education will be delivered in the future." Wharton is offering a basic finance course for non-financial managers. Carnegie Mellon University is serving up a program on the management of technology and information. Pennsylvania State University has a program on human resources.

For companies, schooling by satellite is clearly efficient. Electronic Data Systems Corp., which already has registered "several hundred" of its managers for these satellite programs, views them as a way to offer executive education to far greater numbers of its employees. "Cost is an important advantage to this," says Robert H. Keahey, director of professional development at EDS. "More important than that is the variety of universities and topics we will be able to offer a very large audience. It would be impossible to send as many people at EDS to universities for these courses."

The first of Westcott's 13 managerial courses went live on Oct. 10.

managers. For the next 20 weeks, they will assemble at 5 p.m. every other Tuesday for three hours of business basics, from understanding financial statements to building and sustaining competitive advantage.

The classes are being broadcast from a studio in Carrollton to office buildings in far-flung locales. In each corporate classroom, managers watch the professor on a video screen and speak to him via a microphone in a keypad on their desks. The pad also can be used to alert the teacher to questions and to punch in answers to queries posed by the professor. Teachers, though, aren't able to see their students—or their dazed looks when they aren't following the lectures. Instead, a "flag" button allows them to anonymously inform the professor that his ideas may be over their heads. A computer screen in front of the teacher lets him know what percentage of the students aren't getting it.

**DRAWBACKS.** For this bit of high-tech education, companies pay a \$2,000 monthly fee and tuition ranging from \$165 to \$800 for each manager they enroll in programs. Westcott supplies all the equipment except the video monitors and sets up the classroom. Westcott's Smith estimates that a company needs to enroll 30 to 50 managers in its courses each year to make the schooling cost-effective. Universities providing the professors receive a royalty of about 10% of the tuition or a negotiated flat fee.

The technology has its obvious limitations. Wharton's Mittelstaedt, an enthusiastic supporter of classes by satellite, believes they probably aren't a good idea for upper-tier executives. "At senior levels, executives learn by interaction," he says. "We sell perspective to them, not skills." George J. Siedel, an associate dean at the University of Michigan, believes that the new technology may be best for what he calls "knowledge dissemination" but not what he refers to as "human development," such as teaching managers how to lead and build effective teams. "I don't think you can get these skills from a talking head on a television screen," he says.

Some corporate directors of executive education agree. "There's a place for it," says Dick Sethe, assistant director of executive education at AT&T,

### Education Via Satellite

The business schools now offering executive education programs via satellite to corporate classrooms:

| INSTITUTION/PROGRAM                                                                                            | START DATE                     |
|----------------------------------------------------------------------------------------------------------------|--------------------------------|
| <b>ASPEN INSTITUTE</b><br>Seminar on "Experience Teaches"                                                      | Oct. 23                        |
| <b>BABSON COLLEGE</b><br>Strategic Planning                                                                    | Dec. 13                        |
| <b>CARNEGIE MELLON</b><br>Manufacturing Excellence<br>Management of Technology                                 | Feb. 5<br>March 7              |
| <b>MASSACHUSETTS (AMHERST)</b><br>Selling Your Ideas<br>Managing for Corporate Creativity<br>Ethical Reasoning | Oct. 17<br>Jan. 22<br>March 13 |
| <b>NORTH CAROLINA</b><br>Leadership Into the 21st Century                                                      | Nov. 20                        |
| <b>PENN STATE</b><br>Human Resource Management                                                                 | Jan. 4                         |
| <b>SOUTHERN CALIFORNIA</b><br>Leading Through Change                                                           | Nov. 16                        |
| <b>SOUTHERN METHODIST</b><br>Mid-Management Program                                                            | Oct. 10                        |
| <b>WHARTON</b><br>Creating Customer Value<br>Finance and Accounting                                            | Nov. 2<br>Nov. 13              |

DATA: WESTCOTT COMMUNICATIONS INC.



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## Special Report

Nor are the best classroom professors always the best TV teachers. "You have to put the right people on the screen or you lose the audience right away," says Karen Arden, who heads

executive education at the University of Southern California. "I don't think this is going to replace classroom learning, but it is going to supplement it."

Indeed, most of the courses are highly compressed versions of longer programs. Wharton's Finance & Accounting for the Non-Financial Manager is usually a four-and-one-

half-day program with 23 hours of instruction costing \$4,550. The satellite version will be a trio of three-hour segments for \$600, requiring Wharton significantly scale back course content.

Even so, the satellite classroom may make business courses from professors at the top schools far more accessible to managers, no matter where they are. It's likely to dramatically alter the face of executive education—and extend the work day for many harried managers.

By John A. Byrne in New York

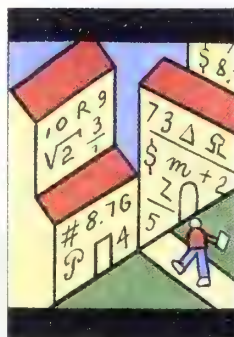
## The 20 Largest Institutions For Executive Education

| SCHOOL                                                    | ANNUAL REVENUES<br>MILLIONS | FIVE-YEAR<br>GROWTH | CUSTOMIZED<br>PROGRAMS* | PROGRAMS<br>OFFERED | SURVEY DETAILS                                                                                                                                  |
|-----------------------------------------------------------|-----------------------------|---------------------|-------------------------|---------------------|-------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>ASHRIDGE MANAGEMENT</b><br>Hertfordshire, Britain      | \$16.1                      | 8%                  | 47%                     | 110                 | Deans rank Ashridge in top 10 for custom programs; big clients include Unilever, Guinness/United Distillers, and Volkswagen.                    |
| <b>CENTER FOR CREATIVE LEADERSHIP</b><br>Greensboro, N.C. | 23.7                        | 57                  | 34                      | 28                  | Hands-down winner among nonbusiness schools for most innovative and creative programs; Kraft, Glaxo, and Motorola are major users.              |
| <b>COLUMBIA</b><br>New York                               | 7.0                         | 0                   | 25                      | 39                  | Rated highly for general management, marketing, and custom courses; top clients include AT&T, American Cyanamid, Nynex.                         |
| <b>CRANFIELD</b><br>Cranfield, Britain                    | 12.9                        | 105                 | 41                      | 152                 | Racks up more revenues than more prestigious rival London Business School; boasts custom programs with AT&T, and British Telecom.               |
| <b>DUKE (Fuqua)</b><br>Durham, N.C.                       | 9.1                         | 44                  | 60                      | 76                  | Ranked No. 2 provider of custom programs and gains kudos for its program on telecom strategy; major users include Eli Lilly, Ford Motor.        |
| <b>HARVARD</b><br>Boston                                  | 30.1**                      | 20**                | 5**                     | 28                  | Deans say it's No. 1 in general management courses; now doing custom programs for Johnson & Johnson, Becton Dickinson, Wyatt.                   |
| <b>IMD</b><br>Lausanne, Switzerland                       | 23.5                        | 2                   | 44                      | 25                  | Ranks among top 10 providers of custom programs; major clients include Ciba-Geigy, Nestlé, Tetra-Laval, Union Bank of Switzerland, Heineken.    |
| <b>INSEAD</b><br>Fontainebleau, France                    | 37.0                        | 42                  | 39                      | 124                 | Deans rate Insead No. 8 in general management programs, praising international business and strategy courses.                                   |
| <b>LONDON BUSINESS SCHOOL</b><br>London                   | 9.9                         | 34                  | 50                      | 13                  | Gains plaudits for courses in finance; boasts custom programs with Heineken, Apple Computer, Johnson & Johnson, and Wellcome.                   |
| <b>MICHIGAN</b><br>Ann Arbor                              | 21.5                        | 53                  | 10                      | 63                  | Deans say its Global Leadership Program is most innovative among all B-school offerings; ranked No. 3 in general management; No. 1 in HR.       |
| <b>MIT (Sloan)</b><br>Cambridge, Mass.                    | 8.3                         | -7**                | 20                      | 42                  | Only top school with falling revenues, Sloan is reshaping its executive education strategy; major users include AT&T, Boeing, Price Waterhouse. |
| <b>NORTHWESTERN (Kellogg)</b><br>Evanston, Ill.           | 14.0                        | 75                  | 35                      | 42                  | Deans rank it No. 1 in custom and marketing programs; No. 2 in general management; top clients include AT&T, Hewlett-Packard.                   |
| <b>PENNSYLVANIA (Wharton)</b><br>Philadelphia             | 25.0                        | 257                 | 55                      | 100                 | Ranked No. 1 in finance, No. 3 in custom courses, and No. 5 in general management; program on "Ambiguous Authority" rated innovative.           |
| <b>PENN STATE (Smeal)</b><br>University Park, Pa.         | 4.2                         | 17                  | 40                      | 38                  | Has aggressively moved into custom field, gaining top 10-ranking in the area; among key users are AT&T, Petróleos de Venezuela, Aramark.        |
| <b>SOUTHERN CALIFORNIA</b><br>Los Angeles                 | 4.4                         | 75                  | 39                      | 35                  | Among new offerings are "Overcoming Resistance to Change" and "Customer-Focused Marketing"; doing custom programs for Times Mirror.             |
| <b>STANFORD</b><br>Stanford, Calif.                       | 6.9                         | 103                 | 2                       | 10                  | Deans rank Stanford No. 6 in general management; major users include Amoco, British Petroleum, Hewlett-Packard, AT&T, and Pacific Telesis.      |
| <b>THUNDERBIRD</b><br>Glendale, Ariz.                     | 6.0                         | 900                 | 55                      | 28                  | Boasts tenfold rise in revenues since 1989, largely due to custom programs for IBM, Upjohn, Motorola, Phelps Dodge, and SGS Thomson.            |
| <b>UCLA (Anderson)</b><br>Los Angeles                     | 8.0                         | 186                 | 29                      | 26                  | Gains praise for programs in health care; has launched new programs in leadership and corporate renewal; among big users are Hughes, TRW.       |
| <b>WISCONSIN</b><br>Madison                               | 4.5                         | 72                  | 11                      | 130                 | Rapidly growing executive business counts Harley-Davidson, Consolidated Papers, and CUNA Mutual Insurance among major users.                    |
| <b>VIRGINIA (Darden)</b><br>Charlottesville               | 10.5                        | 40                  | 29                      | 45                  | Deans rank Darden No. 4 in general management, No. 5 in custom programs; wins praise for change-management programs.                            |

\*Percent of revenues from programs designed specifically for client companies

\*\*BW estimates

DATA: BUSINESS WEEK SURVEY OF EXECUTIVE EDUCATION DE  
(RESEARCH BY ELIAS LEVENS)



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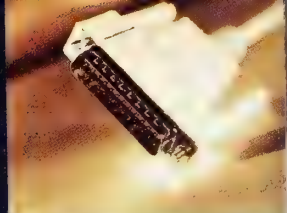


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## Special Report



**TRUEX:** First surprise, then enlightenment

taught through quirky group exercises and an examination of individual's strengths and weaknesses. "Leadership is something we believe resides in almost everybody as a potential, and a better understanding yourself can improve your way of leading," says Robert J. Lee, president of the center.

Though heavy on psychobabble and light on management theory, the center's Leadership Development Program is widely considered to be one of the most innovative executive education experiences on the market. Since 1974, more than 38,000 managers from all over the world have gone through the often-humbling experience,

their companies paying \$4,000 each for the privilege. Alumni say the program boosts self-confidence, helps managers put more balance into their lives, and teaches them to become more effective at work and at home.

**VETERAN SELF-IMPROVER.** For Truex, a New York City-based senior director of national accounts for Sanofi Winthrop Pharmaceuticals, the program is a welcome break from the day-to-day demands of his job. Forty-nine, he has been working in the pharmaceutical industry as a salesman, marketing researcher, and pricing strategist for 18 years, ever since gaining his MBA from the University of Illinois in 1982. Truex is a hard-driving achiever and a self-made professional. Son of a West Virginia coal miner, he worked as a barber in his early 20s while attending night classes at a local community college. Excited by chemistry, Truex went on to earn a PhD in biochemistry at West Virginia University before getting his MBA.

Throughout his corporate career, Truex never lost his love for education. Truex is something of a management-education

# HOW'M I DOING?

This creative-management program uses tough love

It's not that C. Richard Truex was expecting rave reviews from his boss and colleagues. But the executive with pharmaceutical company Sanofi Winthrop Inc. certainly didn't think he would be blasted for being indecisive and not forceful enough in his job.

As he read through the results of a 360-degree evaluation in a classroom filled with strangers in Greensboro, N.C., he felt hurt and misunderstood. "I thought I was decisive when I needed to be," says Truex. "It was a real shock to me to find out I wasn't."

Welcome to Leadership 101, a boot camp for wannabe leaders at the Center for Creative Leadership. Truex is one of 22 managers—3 women and 19 men—who recently spent six days analyzing themselves and how they interact with their colleagues. The goal: to transform themselves into creative leaders, not mere functional managers.

Leadership, of course, has been a hot topic in management circles for years, and the center has been the hottest place to learn it. The center believes that leadership can be nurtured and

## Diary of a Leadership Warrior

*What's it like to go through the Center for Creative Leadership's \$4,400 flagship program? Some 22 managers recently experienced the joys and pains of the six-day adventure, dubbed the Leadership Development Program.*

**SUNDAY** Interview person next to you and then introduce him/her to group. Take IQ and psychological tests, and participate in group exercises.



### MONDAY

Receive "Valentine from home"—feedback from managers, peers, and direct reports; toughest day for many.



(continued on page 74)

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tion veteran, typically attending one program a year. This is his first time at the center, which is no corporate country club. The 20-acre campus is filled

## Special Report

with trees and grass, but the classrooms are sparse, the corridors eerily quiet. And buffet meals are served in a cafeteria that could very well be in a high school.

**"LIKE THE WIZARD OF OZ."** Truex' fellow students are from a wide range of backgrounds, from a Prudential Insurance Co. sales director to a U.S. Army manager of maintenance. Unlike most of them, who arrived at the center on Saturday, Truex took an early flight from Newark, N.J., on Sunday morning and went straight to class for introductions, group exercises, and IQ and psychological tests. The main classroom, where three long tables formed a U-shape, featured an observation window in the back. Participants joked that they felt as though they were in CIA headquarters. In fact, two trainers from the intelligence agency were observing the program from behind the mirror.

What they saw on Sunday was lots of confusion. In one session, Truex' group argued when it had to compile a list of the ideal characteristics for a leader for Earth II—a new planet to which a portion of the earth's population was relocating because of dwindling natural resources. When a participant took too much time, a booming voice from behind the mirror filled the room: "Time is up!" Truex, who as a market researcher had surreptitiously watched focus groups, wasn't disturbed by it—but many of his classmates were. "It was like the Wizard of Oz," jokes one manager stunned by the voice.

Far more disturbing to many was Monday's "Valentine from home"—a

bound packet of evaluations of all the participants prepared before their arrival in Greensboro by a boss, four peers, and six direct reports. The assessments asked colleagues more than 200 questions, from whether a manager was viewed as abrasive or encouraging, to whether he "takes charge when trouble comes" or "has left a trail of bruised people."

When the evaluations were handed out, the room fell silent. Managers, clad in khakis and polo shirts, sat highlighting all their strengths with green markers and all their weaknesses in pink. Truex quickly found himself marking in pink issues that focused on decision-

**"The reason I'm not decisive is that I won't give myself permission to be wrong," says Truex**

making and assertiveness. "Forcefulness was a question mark in the back of my mind," concedes Truex. "It's confirmed that I am not forceful, and it is an area that I have to work on."

Throughout the week, these two themes continued to crop up. In one assignment, managers were asked to pretend they were caught in a blizzard while hiking. The group theoretically made it back to their Ford Windstar, only to crash it into a rock. Stranded 35 miles from the main road, members had to debate which of 15 items, from beef jerky to a shotgun, were critical to their survival.

Truex, however, grouched that he wasn't getting heard by the other members of his group. One manager told him he didn't speak up enough. Al-

though angered initially, Truex later conceded it's true. "I'd make a point and just let it drop off the table."

The Outward Bound-type activities on Wednesday afternoon were also frustrating. Again, Truex found it difficult to get his opinions through to fellow group members. "It was these old men competing to see if they could yell the loudest to win the ego fight," Truex complains.

After four long days of intense group sessions, sprinkled with lectures and still more test results, yet another day of reckoning arrived. The two trainers who guide participants through the week, call Thursday "feedback day."

From day one, two to the fellow students anonymously observe each manager. On feedback day, they deliver their comments.

His peers again confirmed what he now already knew. It wasn't until Truex sat down for nearly four hours with a clinical psychologist, however, that it began to make some sense. The psych-

ologist's assessment: Truex is a perfectionist who doesn't like to make mistakes. "The reason I'm not decisive is that I won't give myself permission to be wrong," Truex says.

Back at his desk on Oct. 2, Truex confronted an overflowing in-basket and a ton of telephone calls. Still, he managed to find time to ask his boss if he could sit down together and find some noncrucial areas where Truex can experiment with making quicker decisions. "I am going to try some thing I haven't tried before," he says. "I'm going to take more risks." Though Truex will probably never be the person who screams the loudest, that's a crucial first step.

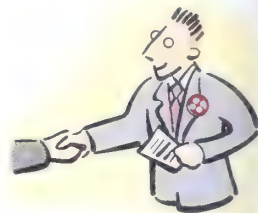
*By Lori Bongiorno in Greensboro, N.C.*

## Diary of a Leadership Warrior (continued)

**TUESDAY** Breakout groups are videotaped as they rank the importance of items they'll need to survive an imaginary blizzard. Later watch video and critique one another.



**THURSDAY** Get one-on-one counseling based on results of several hours of preprogram tests. Give and get feedback from colleagues.



**WEDNESDAY** Outside activities include leading blindfolded partner through construction sites and stairwells.



**FRIDAY** Prepare goals and share one with group; receive diploma signed by entire group. Rush to catch plane home.



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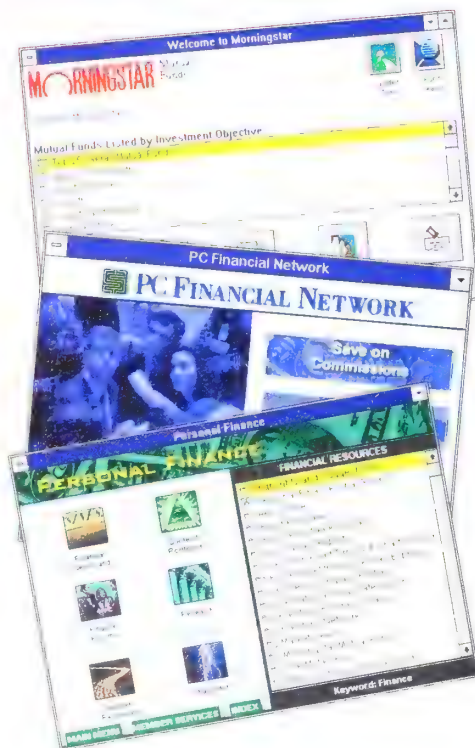
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## THE YELPING OVER LABOR'S NEW TACTICS

Businesses file RICO charges and run to Congress for help

When Bayou Steel Corp. faced down a 1993 strike by bringing in 400 replacement workers, the United Steelworkers of America went on a hiring binge of its own. The USW brought in 7 New York investment bankers, Washington environmental consultants, and 7 others in Louisiana, Tennessee, and New York. The new team blanketed you with a blizzard of paper: frightening letters to potential investors, tomb-raider ads in the financial press, submissions to the Securities & Exchange Commission, and hundreds of requests for regulatory crackdowns at the company-based in La Place, La. "It's been a pervasive campaign," says a beleaguered Richard J. Zalez, Bayou's chief financial officer. "The costs have been awesome."

With the power of strikes waning, unions in recent years have tried to combat management with such tactics—often called corporate campaigns. In August, Bayou joined a growing number of companies that have filed racketeer suits against unions ended in such campaigns. Meanwhile, the Chamber of Commerce and other business groups are pushing the Republican majority in Congress to pass legislation to limit unions' powers. The outcome on either front isn't clear. But there are likely to be more clashes on the issue, as new leaders are ed to take over the AFL-CIO this month vow to expand the use of corporate campaigns as part of labor's strategy for the late 1990s.

Although corporate campaigns started more than 15 years ago, most large unions have used such tactics in the late 1980s, as the fear of replacement workers chilled members' eagerness to strike. In recent years, many labor bat-

tles have involved nontraditional union efforts (table). For instance, the steelworkers sent fired Firestone employees and their families to Tokyo, where they engaged in street theater outside Bridgestone/Firestone Inc. headquarters to embarrass managers in their home country.

To strike back, companies are using a powerful weapon: the Racketeer Influenced & Corrupt Organizations Act. Management lawyers argue that RICO should apply, claiming unions' campaigns often aim to take control of the company or even sink it. Bayou's RICO filing alleges that the steelworkers' actions constitute a pattern of behavior that amounts to extortion. The USW's campaign "is designed to put Bayou Steel out of business," charges the company's

**STREET THEATER: FIRED  
FIRESTONE WORKERS  
TRY TO EMBARRASS  
COMPANY MANAGERS  
IN TOKYO**



**AT FOOD WORKERS'** suggestion, former Food Lion clerks tell ABC TV lurid stories—false ones, says the company—of efforts to recondition rotten food. The supermarket chain files a racketeering suit against the union.

**THE USW** rains on Bayou's Wall Street road show, sending a dire letter to potential investors. Bayou is forced to raise its dividend—and files racketeering charges.

**TEAMSTERS** mount proxy fights at large trucking companies during 1994 bargaining. Industry groups are pushing for legal curbs on union shareholder actions.

DATA: BUSINESS WEEK

outside attorney, William A. Brewer III.

Management hasn't yet won a RICO suit against a union—and may never do so. After all, say some labor lawyers, corporate raiders routinely mount takeover efforts, and environmental groups constantly urge regulatory agencies to pursue companies. Companies haven't yet explained why such behavior would be illegal just because the adversary is a union or an employee of the company involved, the lawyers say.

Still, racketeering suits can tie up unions in court and cost them a bundle. And several companies have made it to the discovery stage of a RICO trial before reaching settlements, as Frank A. Lorenzo's Texas Air Corp. did in the late 1980s. "Every time there's a new union action, [Bayou] will amend the suit to keep it from being dismissed," says Jerry Fernandez, head of corporate campaigns at the USW.

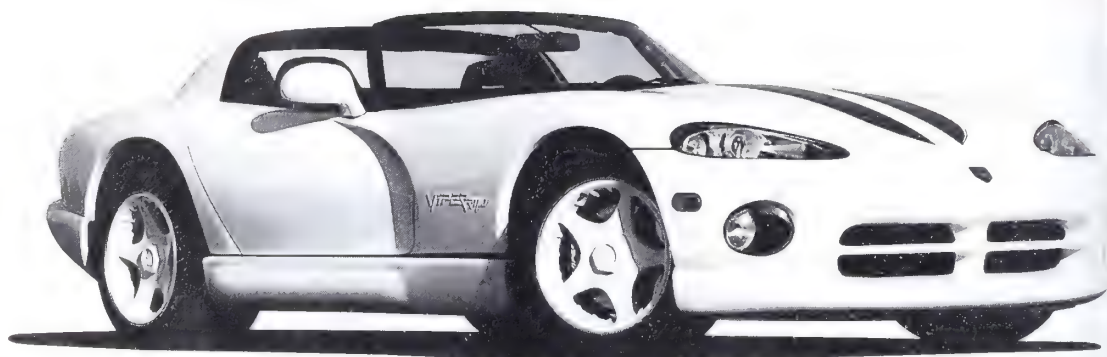
**"PURE HARASSMENT."** Business groups hope that Washington can offer more immediate relief. Their main target: the growing number of labor proxy battles, which have quadrupled since 1992, to 70 last year. Unions often act because their pension funds are unhappy with a stock's performance. But sometimes they have other motives. Last year, the Teamsters sponsored proxies over corporate-governance issues, such as poison pills, at the three largest trucking companies—and did so right in the middle of national bargaining talks.

In August, a coalition of business groups asked Congress to curb union proxies. They proposed changing SEC regulations to let companies involved in bargaining or organizing campaigns exclude union-sponsored resolutions from annual proxy statements. "They're nothing but pure harassment," fumes American Trucking Assns. President Thomas J. Donohue. The business groups also want to limit National Labor Relations Board injunctions.

Management isn't likely to score any quick victories in Washington, where the budget tops the agenda. Still, business' strategy seems sure to tie up unions in the courts and before congressional committees, leaving them less time and money for their punishing corporate campaigns.

By Stephen Baker  
in Pittsburgh





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Cover Story

# BLIND AMBITION

How the pursuit of results got out of hand at Bausch & Lomb



## BY MARK MAREMONT

**B**a dan. In Cantonese, the words mean "white sheet." But for employees at Bausch & Lomb Inc.'s Hong Kong operation, they had another meaning: According to high-ranking sources familiar with the unit, *ba dan* signified a white invoice with phony sales recorded on it. And there were plenty.

During the late 1980s and early 1990s, Hong Kong was the hub of B&L's international division, often racking up annual growth of 25% as it rocketed to about \$100 million in revenues by 1993.

Trouble was, in recent years, some of the reported sales were fake. Under heavy pressure to maintain its phenomenal record, sources allege, the Hong Kong unit would pretend to make big sales of Ray-Ban sunglasses to distributors in South Asia. But the goods would not be shipped. Instead, the *ba dan* invoices, which B&L headquarters never saw, would instruct staffers to send the goods to an outside warehouse in Hong Kong. Later, some B&L sales managers would try to persuade distributors to buy the excess. And some of the sales, sources suspect, may also have been funneled into the gray market; buyers could profit by shipping them to Europe or the Middle East, where wholesale prices were higher.

But by mid-1994, Hong Kong was having trouble keeping up its juggling act. Tipped off by falling revenues and soaring receivables—since no one was paying for many of the glasses listed as sales—B&L sent a team of auditors to Hong Kong. They discovered significant irregularities, including half a million pairs of sunglasses stashed in a warehouse.

B&L's longtime chairman and chief executive, Daniel E. Gill, declines to comment on the Hong Kong problems; the company says only that it uncovered "violations of company policies." But in the audit's wake, Y.H. Chan, president of B&L's Asia-Pacific Div., took early retirement, and several other managers also left as part of the cleanup.

Meanwhile, in late 1994, the Securities & Exchange Commission started combing through the books at another B&L unit, its U.S. contact-lens division. The SEC investigation was triggered by a *BUSINESS WEEK* article (Dec. 19, 1994), which revealed that the lens division might have improperly inflated sales and profits in 1993 by shipping huge quantities of unwanted lenses at yearend to its distributors, while assuring many they wouldn't have to pay until they sold the lenses.

The double-barreled problems lay behind B&L's swift fall from financial grace: After 12 straight years of double-digit growth in sales and earnings from continuing operations (excluding one-time events), B&L blandly announced that excess distributor inventories would slash 1994 profits. B&L's continuing earnings

**STRONG-WILLED CEO:** *Gill rejects suggestions that Bausch & Lomb's culture is flawed*

## Isolated Aberrations – Or a Way of Business?

*Current and former execs say that under CEO Dan Gill, maintaining Bausch & Lomb's double-digit sales and earnings growth was all-important, creating pressures that led to unethical behavior throughout the company:*

**HONG KONG** B&L's Hong Kong unit allegedly inflated revenues by faking sales of Ray-Ban sunglasses to real customers. Some of the glasses were allegedly then sold at cut-rate prices to gray-market dealers. B&L auditors discovered policy violations last year, and Gill appointed new local managers.

**MIAMI** By accepting cash payments and third-party checks, a Miami warehouse may have indirectly helped launder drug money until mid-1990. Senior B&L managers tolerated the lucrative trade, say former executives. B&L declined comment.

**CONTACT LENSES** Under pressure to beat sales targets in 1993, contact lens managers shipped products that doctors never ordered and forced distributors to take up to two years of unwanted inventories. These practices appear to violate acceptable accounting standards and have led to an SEC investigation. B&L blames the problems on overaggressive division executives.

**GRAY-MARKETEERING** Forced to meet inflated sales goals, many U.S., Asian, and Latin American managers knowingly sold contact lenses and Ray-Bans to gray-market distributors, creating a huge gray-market problem for B&L. The company says such sales violated policy and denies its practices led to the problem.

DATA: BUSINESS WEEK

fell 54%, to \$88.5 million, on sales down slightly, to \$1.9 billion.

As the bad news piled up, Gill, 59, has worked to reassure staffers and investors alike. He has installed new managers in the contact-lens unit and in Southeast Asia. He has replaced B&L's chief financial officer and has announced measures to strengthen internal controls. The problems, Gill insists, were isolated aberrations. In 1993, he says, "two of our major operating units had difficulties, and what they did was wrong. The minute we got any wind of it, we sent auditors in. We recognized that we needed new leadership." Now, he adds, "our performance is growing back, and we're very proud."

**EXPEDIENCY.** Yet a six-month *BUSINESS WEEK* investigation suggests that the 1993 events were hardly isolated. They were direct, though unintended, byproducts of a corporate culture gone badly awry. The investigation involved extensive interviews with more than 50 current and former executives, including representatives from numerous B&L divisions spread across the world.

Their tales provide a remarkably consistent picture: Driven by Gill's fierce insistence on achieving double-digit annual profit growth, B&L's managers by the early 1990s increasingly resorted to what was expedient—often at the expense of what constituted sound business practice or ethical behavior. They gave customers extraordinarily long payment terms, knowingly fed gray markets, and threatened to cut off dis-





tributors unless they took on huge quantities of unwanted products. Some also shipped goods before customers ordered them and booked the shipments as sales, a possible violation of recognized accounting practices. For a period, the company also turned a blind eye to lucrative Latin American sales that may have indirectly

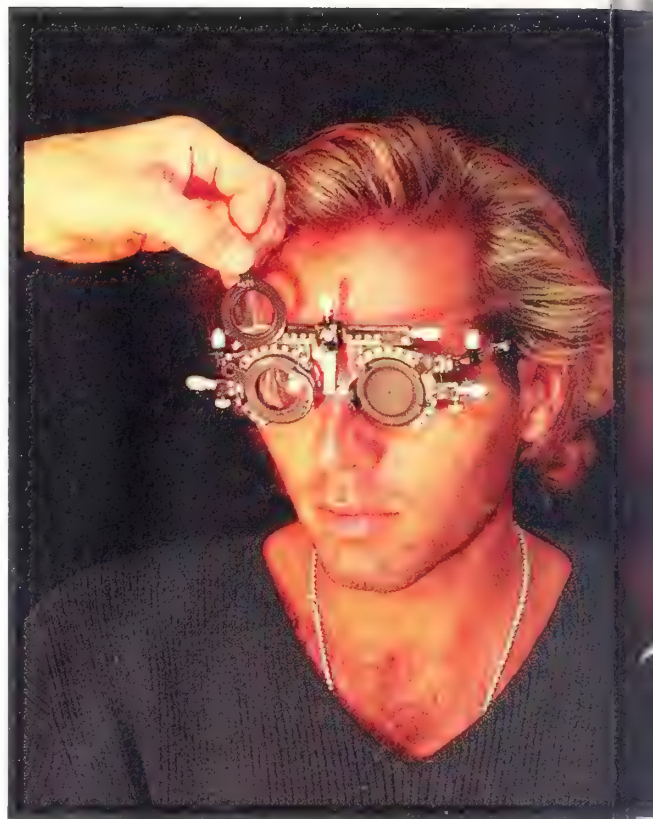
## Cover Story

aided money laundering (page 92).

To be sure, B&L's performance-oriented ethos delivered outstanding results for many years. But by the early 1990s, when the company's markets slowed at the same time that several acquisitions soured, B&L's culture was a train wreck waiting to happen. The derailment finally took place in 1993 and 1994, when B&L maintained its steep growth targets even as markets stalled.

According to internal B&L financial documents obtained by BUSINESS WEEK, the contact-lens and Hong Kong units weren't the only ones artificially loading up distributors in 1993. Executives in the U.S. sunglass division, Italy, Latin America, and in the Interplak oral-care unit also stuffed distributors with excess goods. Interplak executives, for example, fattened fall sales by giving buyers until the following spring to pay. As a result, the unit's accounts receivable nearly tripled from June to December.

Although the soaring receivables should have been a clear sign to Gill and other top executives that the growth could not be sustained, B&L's internal documents show that the 1994 corporate plan called for most of B&L's largest units to turn in further double-digit gains. When the inevitable collapse arrived, it was bloody indeed. In 1994, the documents



## The company's culture mirrors the boss: Tenacious, demanding

show, 6 of the company's 15 largest divisions recorded sales far below plan—and far below actual 1993 sales (page 81).

Gill and other top executives vehemently deny that the cascade of difficulties in one year reflects wider problems with the company's culture. "It was no accident that Bausch & Lomb had an absolutely outstanding record for the preceding 11 years," says Gill. "We don't feel at all, given that track record, that it's a fundamental cultural issue."

Instead, in explaining what went wrong in 1993, Gill zeroes in on two top executives who were new to their posts, hinting that their inexperience may have contributed. Both have since left B&L. One, Peter Stephenson, was an outsider who lasted only a year as CFO. The other, Ronald L. Zarrella, was a nine-year company veteran who had headed B&L's fast-growing international division before becoming president and chief operating officer in early 1993. Zarrella left B&L late last year to become head of North American marketing for General Motors Corp. Zarrella declined comment; Stephenson could not be located.

**RISEING STAR.** B&L's intense focus on the bottom line and quarterly results is hardly unique: Many of Corporate America's most successful companies share similar goals. Good managers attempt to balance that orientation with effective controls and compensation plans that also reward practices that pay off in the longer term. B&L's saga shows what happens when those countervailing forces aren't strong enough. "People spend their time trying to figure out what kind of game to play to make the numbers, not how to satisfy the customer or save money," says John P. Kotter, a Harvard business school professor. "The tendency is for people to step over lots of lines."

When Dan Gill came to Bausch & Lomb in 1978 to head its fast-growing soft contact-lens division, the stodgy manufacturer of optical equipment, eyeglass lenses, and contact lenses had just \$442 million in revenues. Gill, a rising star from

Abbott Laboratories Inc., made his mark: Contact-lens profits soared, and Gill won the president's job in 1980. The following year, he was named CEO and chairman.

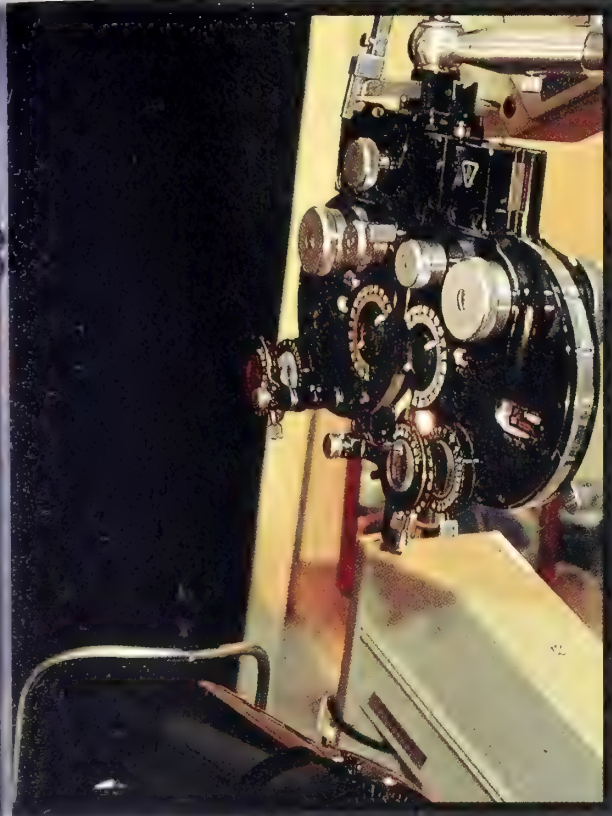
Young and ambitious, with a salesman's charm and a financial analyst's head for numbers, Gill wasted little time. He sold several inefficient optical businesses while bolstering growth with acquisitions and a push abroad. "Dan did a marvelous job of refocusing the company," recalls Stephen Kelbley, CFO from 1984 to 1991.

But from the beginning, some executives questioned how B&L's strong growth was achieved. In 1981, Mark B. Logan was recruited from Becton, Dickinson & Co. to head a hose operations, including the soft-lens division that Gill had been running. Logan soon wondered why lens sales were so slow for the first two months of every quarter. He discovered that under Gill, the division had run big promotions at the end of every quarter to pump up sales. Eye doctors had learned to wait for those deals. Logan says Gill made no bones about it. "I needed to be chosen CEO," he recalls Gill saying. "I did what I had to do." Gill doesn't recall the incident.

The culture Gill created at B&L is a mirror image of his tenacious, demanding—and very numbers-oriented. Gill bears his career as an auditor and still closely examines each division's financial reports every month. One executive says he often received handwritten notes from Gill on issues such as inventory buildups. "He has a tremendous ability to stay on top of financial details," says this former executive.

Achieving double-digit annual growth was Gill's foremost goal. Each division was usually expected to post substantial annual gains. "Each year, the top executives would agree on what number they wanted to make," recalls Harold Johnson, the longtime head of the contact-lens unit, who retired early this year. "The numbers would be divided out by operating units and then assigned. [The president] would





**TROUBLE:** Contact-lens wearers charged B&L with wildly divergent pricing in a 1994 lawsuit

through clearly at meetings of B&L's top two dozen executives, when Gill or his president drilled those who fell even slightly behind. At one teleconference, re-

calls an insider, the then-head of European operations was raked over the coals by Zarrella because currency fluctuations were hurting profits that were on target in local-currency terms. "Ron kept going back at him, saying 'That's what you signed up for. Do you want me to go to the analysts and say we can't make the numbers?'" says this source.

B&L's compensation structure was also reshaped in a way that buttressed the all-important message. Gill denies this, arguing that bonuses took account of many factors, such as asset management. But former executives say that division heads might get only a paltry bonus if they fell even 10% shy of yearly earnings targets, while beating them brought hefty payouts. And although a small weight was given to asset-control measures such as receivables and inventories, "you could miss your asset objectives by a mile and still get a big payday," says one former executive.

**PANIC ATTACKS.** Nowhere were the true corporate priorities clearer than in the weighting of Gill's own bonus plan: 30% depended on sales growth, 30% on earnings growth, and 30% on return on equity, another earnings-related measure. Improvement in customer satisfaction rated just 10%. At that, Gill's pay structure differs little from most U.S. CEOs'.

At the same time, Gill rarely discussed specific actions that a division might take to rectify a shortfall. "Make the numbers, but don't do anything stupid," was a famous Gill line. Many executives say they read the message differently. "I'd walk away saying, 'I'd be stupid not to make the numbers,'" says one ex-marketing executive.

The signals sent from the top led some to cut corners, several former managers say. Some divisional presidents, they say, began using tactics that were costly for the company but which maximized their own bonuses. One favorite was extending unusually long credit terms to customers in exchange for big orders. And believing their careers were on the line every quarter, B&L managers also lived in fear of "Red Ball" day. It was so named because of the red dot that marked the last day of B&L's 13-week fiscal quarters on employee calendars, which always fell on a Friday or Saturday. "Mini" Red Ball days also fell at the end of every month. As Red Ball day approached, "you'd see panic-stricken account managers offering money off, or extra 30 to 60 days' payment terms," says a former Ray-Ban marketing exec. Such moves boosted volume but hurt margins: B&L's customers, says the Ray-Ban

## very numbers-oriented

to me and say, 'Here's your number.'" Once the goals were set, Gill and other top executives rarely accepted excuses for shortfalls; even Gill's backers agree that making the numbers was key. "Once you signed up for your target number, you were expected to reach it," says former President Thomas C. McDermott, who left B&L in early 1993.

Gill denies that numbers drove B&L's culture to an unreasonable degree or that sales and earnings goals became all-consuming. "That's simply not true," he says. He says goals were set in negotiations with managers, and sometimes adjusted downward if they weren't being met. He adds that many executives have been promoted even after missing targets. But former executives say the priorities came

## Missing the Mark

B&L insiders say that aggressive sales practices left distributors overstocked at the end of 1993. But CEO Gill approved even higher sales and earnings targets for 1994. When distributors balked, sales in many divisions collapsed.

| DIVISION                       | 1993   | 1994<br>Planned | 1994<br>Actual | DIVISION                           | 1993  | 1994<br>Planned | 1994<br>Actual |
|--------------------------------|--------|-----------------|----------------|------------------------------------|-------|-----------------|----------------|
| MILLIONS OF DOLLARS            |        |                 |                | MILLIONS OF DOLLARS                |       |                 |                |
| <b>TOTAL BAUSCH &amp; LOMB</b> |        |                 |                | <b>ORAL CARE</b>                   |       |                 |                |
| SALES                          | 1872.2 | 2051.9          | 1850.6         | SALES                              | 68.8  | 73.0            | 50.8           |
| OPERATING EARNINGS             | 300.9  | 344.7           | 168.8          | OPERATING EARNINGS                 | 2.6   | 4.2             | -10.3          |
| <b>US EYEWEAR</b>              |        |                 |                | <b>MIRACLE EAR**</b>               |       |                 |                |
| SALES                          | 190.1  | 200.0           | 153.5          | SALE                               | —     | 57.9            | 37.3           |
| OPERATING EARNINGS             | 42.3   | 48.6            | 19.7           | OPERATING EARNINGS                 | —     | 2.3             | -12.9          |
| <b>US CONTACT LENS</b>         |        |                 |                | <b>CANADA AND LATIN AMERICA</b>    |       |                 |                |
| SALES                          | 151.0  | 176.0           | 85.8           | SALES                              | 126.1 | 154.0           | 113.4          |
| OPERATING EARNINGS             | 16.8   | 20.5            | -61.7          | OPERATING EARNINGS                 | 17.8  | 27.3            | 6.4            |
| <b>ASIA-PACIFIC</b>            |        |                 |                | <b>EUROPE, MIDDLE EAST, AFRICA</b> |       |                 |                |
| SALES                          | 148.9  | 169.7           | 107.8          | SALES                              | 246.5 | 249.0           | 240.6          |
| OPERATING EARNINGS             | 34.6   | 46.8            | 4.0            | OPERATING EARNINGS                 | 60.7  | 60.3            | 53.0           |

\*Loss \*\*Acquired during 1993 DATA: COMPANY REPORTS



And Ray-Ban  
sunglasses on display  
in Hong Kong (below)

Although top executives frowned on the practice, the division sales managers actively encouraged it. "A lot of salespeople were getting bonuses based on how much their distribution was diverted," says this executive. Nor was B&L U.S. alone: B&L's Latin America managers, too, encouraged diversion. The Miami-based unit supplied the New York-area distributors, for example, and shipped most of the goods to Europe. Says Armando Perez-Gil, a former sales executive in the division: "The president was sure to make the numbers was such, everybody was shipping to anyone." B&L says that any support of gray marketing by managers "has been and will be dealt with as a clear violation of company policy."

**THE STINGS.** One solution would have been to switch to global proce-

[illegible]

Sources close to B&L allege that Hong Kong head Y.H. Chan abetted gray-market Ray-Ban sales. In one deal, Chan allegedly sent buyers who wanted cheap sunglasses to distributor Chamberyan Thom. Chamberyan allegedly sold model No. L0205 for \$25.13, while B&L sold it to local retailers for around \$32. Thousands of sunglasses intended for Hong Kong shops ended up in Italian optical stores. Chamberyan Thom denies such sales.

The lumping of orders into a few frantic days each month also made B&L's distribution operations woefully inefficient. Its sunglass distribution center in San Antonio, Tex., stayed open around the clock the last few days of every month in recent years. That meant hiring up to 35 temporary workers, while staffers racked up huge overtime. "We'd ship 70% of the month's goods in the last three days," says a former operations manager. "The hourly workers must have thought we were nuts."

By overstocking distributors with cut-price products, B&L was partly responsible for another big headache: a flourishing

management, but Gill says such a change couldn't be made abruptly. Instead, B&L turned to its internal security department, staffed by ex-Secret Service and police officers. So even as some managers were secretly encouraging diversion, B&L security staffers were setting up elaborate "sting" operations in order to shut the diverting distributors down. The result was a tense internecine battle between regions in which many U.S. distributors lost their licenses.

For years, B&L was able to keep this frenetic juggling act hidden from public view. The high-margin contact-lens-solution unit was growing fast. And Ray-Ban's Wayfarer sunglass style caught fire after being popularized in movies such as *The Blues Brothers*. By 1991, sales and earnings—at \$1.5 a



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# Managers lived in fear of "Red Ball" day—named for red dots marking the end of fiscal quarters on B&L calendars

lion and nearly \$150 million, respectively—had more than tripled in a decade. B&L's shares had risen fivefold, to 58.

With success, Gill took on the trappings of a big-company executive. B&L bought a three-plane fleet and later erected a nicely appointed private terminal at the Rochester (N.Y.) airport. By 1989, Gill obtained a security consultant's report recommending that top B&L execs use the company fleet for all travel, including personal trips. B&L declines to comment.

## Cover Story

Gill began using company planes to reach his home in Florida and a private fishing club in Canada; the value of such trips is included in his income. And Gill commissioned a sparkling new \$70 million headquarters building set to open this month.

B&L's new stature also meant big salary jumps for Gill, who took home \$362,000 in 1981, his first year as CEO. While shareholders did well, Gill did far better: In 1991, he pocketed \$6.5 million, an eighteenfold gain. That was followed by \$5.7 million in 1992. Although a fall in B&L's stock cut Gill's compensation to \$3.2 million in 1993, Gill still came out ahead of many peers. In an annual study comparing CEO pay at 424 large companies, executive pay consultant Graef Crystal found that even after adjusting for company size and shareholder returns, Gill earned more than double the market average. Because of B&L's earnings and stock-price drop in 1994, Gill received no bonus on top of his \$1.1 million salary that year.

B&L's problems were mounting by the early 1990s, though. Growth was slowing in the U.S. and Europe. Gill's strategy of moving beyond optics to a broader range of health products wasn't panning out: Several big acquisitions were either losing money or barely profitable. Ray-Bans were starting to lose cachet. And B&L was steadily losing market share in contact lenses to Johnson & Johnson, which had caught B&L sleeping when it pioneered disposable lenses in 1987.

**NEW PACKAGING.** From the last quarter of 1992 until early 1994, the dealmaking became frantic. To move Ray-Bans, the division tried one end-of-quarter promotion after another. At one point, says one big Ray-Ban distributor, "we had nine months' inventory. I bought extra insurance and sweated a lot at night." In Latin America, too, Perez-Gili says one late 1993 deal in which he loaded six months' worth of Ray-Bans onto a Chilean distributor was all too typical. Gill denies that such distributor-loading took place.

Nowhere did the situation get more out of hand than in the U.S. contact-lens division. Lacking a disposable lens to counter J&J, the unit tried a shortcut. Starting in 1989, it took the same lenses sold since the 1970s and repackaged them as the frequent-replacement Sequence 2 and Medalist brands. But while a pair of the older Optima lenses went for about \$70, the new brands went for as low as \$7.50.

When Optima consumers discovered that they were paying roughly 10 times more for the same product, the move backfired.irate consumers have since filed a class action. "It's a real ripoff," says Tim P. Quinn, one Optima wearer who's suing B&L. "I was led to believe that they were the only lens I could wear." B&L dismisses the suit, contending that price reflects volume discounts for buying more lenses per year. **"QUESTIONABLE."** Meanwhile, the division was churning out new and ever-more-aggressive marketing promotions. It offered eye doctors 90-day payment terms and a 30% rebate if they took a large package of lenses. The division also had a habit of constantly rolling over unpaid bills so that customers wouldn't return unwanted goods for credit. "It was a total mess," says an ex-rep. "You needed a degree in physics to figure out the bills."

The pressure was immense. Sources say managers in the Northeast district ordered reps to simply ship packages worth \$1,600 to \$2,400 containing a new type of multifocal lens to every account that hadn't ordered any. "I was told it would be much better for my career to just ship the product into accounts," says one rep. All told, says another, several

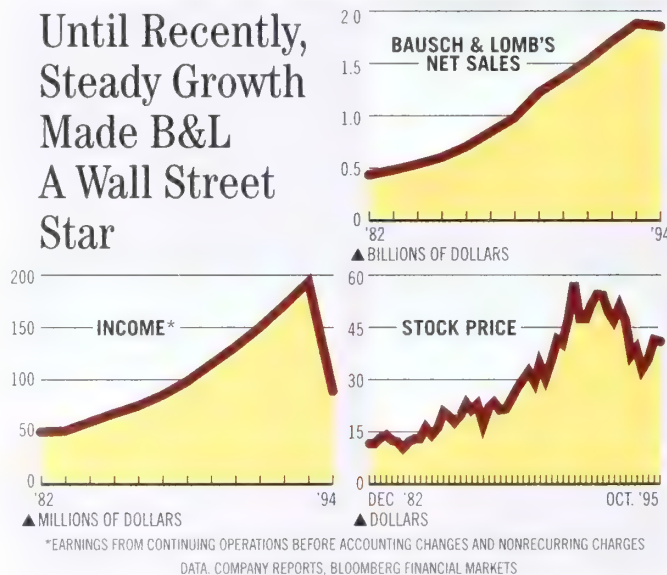
hundred doctors who shipped lenses they didn't order, and the shipments were booked as sales. Accounting experts say booking un-ordered products as revenues apparently violates accounting standards. "It sounds wrong," says Arthur H. Carley, a longtime auditor with Coopers & Lybrand who is now an accounting professor at the Wharton School. Such transactions "appear to be questionable as valid sales."

The worst was yet to come. In mid-December, according to more than a dozen sources, Johnson called about 30 of B&L's U.S. distributors to a meeting and told them they were expected

to take huge new stocks of older Optima lenses—up to a year's worth—and he threatened to sever their distributorships if they refused. However, many distributors were assuaged verbally that they wouldn't have to pay for the lenses if they sold them. All but two agreed, allowing Johnson to log an extra \$23 million in sales in the final days of 1993. But long into 1994, almost all of the unwanted multifocal lenses came back to B&L. And the distributors refused en masse to pay for the huge unwanted Optima inventories. Now, the division's actions are at the core of an SEC investigation into possible accounting irregularities.

Gill and other top B&L executives blame poorly executed marketing plans—and point the finger for the aggressive tactics squarely at Johnson. Although he approved the general strategy, Gill says he had no idea Johnson would ship all those goods in December. Moreover, after the 1993 fiasco, Gill says he discovered that the contact-lens managers "made the decision in April or May that they were going for a maximum bonus." Johnson calls that account "ludicrous." He says both

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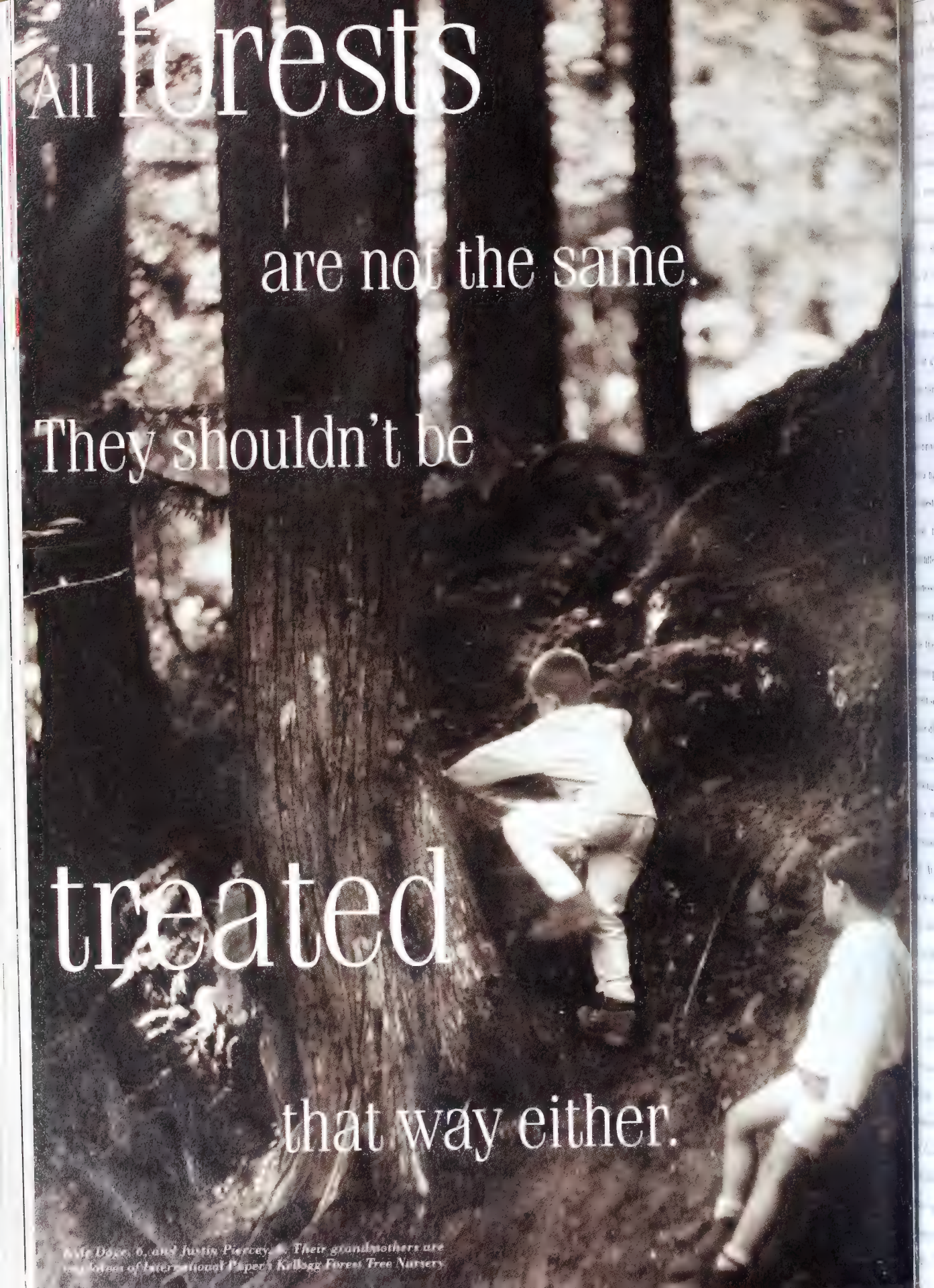
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are not the same.

They shouldn't be

treated

that way either.

*Kyle Dage, 6, and Justin Piercey, 8. Their grandmothers are  
volunteers at International Paper's Kellogg Forest Tree Nursery.*



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and Zarrella knew of and approved the \$23 million in yearend shipments. Indeed, says Johnson, had he really been seeking to maximize his bonus, just half of that giant yearend shipment would have done it. "Either I'm completely out of my mind" to have shipped the whole thing, says Johnson, or "somebody asked for more revenue to make...the budget for the corporation."

## Cover Story

B&L's internal financial documents clearly show the strain of efforts to pump up sales. Receivables rose about 25% in 1993 to hit \$506 million. That equaled 90 days of sales, which accounting experts say is higher than the 45 to 60 days they'd expect. But in B&L's annual report, receivables were shown at just \$385 million. Why? B&L "factored" \$105 million worth of receivables, selling them to a third party to raise cash. B&L argues this is a normal practice that doesn't require disclosure. But Sy Jones, a factoring expert at Coopers & Lybrand, strongly disagrees. "I would consider it required disclosure to footnote the nature of a factoring arrangement and the interest rate being paid."

Yet despite the rising receivables, B&L's internal financial documents show no letup in the pressure for results. Revenues for the division were targeted to rise yet again in 1994, from \$151 million to \$176 million. But with distribution channels chock-full, actual sales for 1994 slid to just \$85.8 million, and the unit posted a \$61.7 million loss.

Indeed, as the 1993 overloading took its toll, many divisions faced the same sharp drop. While U.S. eyewear sales had been budgeted to rise 5% in 1994 to \$200 million, they tumbled to \$153.5 million. Latin America and Canada sank 26% below target, while the oral-care unit lagged by 30%. By June, 1994, Gill warned investors that profits would tumble. B&L's shares fell to around 30, though they've since returned to around 39. But investors weren't told the details behind the biggest can of worms: Hong Kong.

In the fall of 1994, auditors jetted out to Hong Kong from B&L headquarters. The team spent eight months combing through records, grilling staffers, and counting inventory. The man they questioned the hardest was Chan, the longtime head of the Hong Kong operation, which handled sales in most of Southeast Asia. Chan's superb track record had made him a "hero" around Rochester, recalls former President McDermott. In early 1993, Chan was promoted to head all of Asia-Pacific. Facing intense pressure to keep it up, the unit allegedly intensified the *ba dan* trick—

the fake sale of sunglasses that were dumped in warehouses.

Some of those sunglasses would then be sold to legitimate distributors the next quarter. But sources allege that Chan may have been boosting sales by diverting sunglasses to the gray market. Hong Kong was a natural origin point for gray-market activity, because Chan was selling glasses for 10 to 30% below B&L's prices in the U.S. and Europe. In part, low prices were due to local competition and to compensating for high duties in some countries. But sources also say Chan would use his marketing budget to fund secret rebate customers, in effect lowering their buying price.

Ray-Bans seemed to find their way into the gray market at unusually low prices—perhaps with Chan's direct complicity. In either case, those prices allowed buyers to undercut whole prices in Europe and elsewhere. One gray-market dealer told BUSINESS WEEK that he approached Chan personally in early 1992 about buying discounted sunglasses for shipment to Italy and Latin America. Chan directed him to two Hong Kong companies, he says. Invoices provided to BUSINESS WEEK show that one, Chamberyan Thom, offered to sell the Aviator for \$25.13 apiece in early 1992.

At this buyer. During that period, a large Hong Kong optical chain says it was buying the same model directly from B&L for about \$32 to \$34. The gray marketeer says many of the glasses ended up in Italy.

S. L. Chiu, the manager of Chamberyan Thom whose nature is on the invoices denies that Chan referred people to his company for discounted glasses and did not sell such glasses. But he pressed, he added: "We're not doing that now."

In 1994, the Hong Kong unit started to unravel. Legitimate sources say the end came when accounts receivable on the roof, in part because of *ba dan* sales that had been booked to legitimate distributors weren't being paid. Gill declines comment on the allegation. After B&L auditors started the in-depth probe, they found about a half-billion sunglasses worth roughly \$12.5 million piled up in a rented warehouse. How they got there remains in dispute. Gill says that in the face of a weakening economy, Chan simply sold too much inventory to distributors starting in late 1993, then decided without company approval to take back large amounts in September, 1994. Other sources say some of the glasses were indeed returned by customers, but many were the result of faked *ba dan* sales.

Chan retired in late 1994, as did his controller, Jack H. K. Tsang. B&L says it had planned to retire anyone. Neither responded to BUSINESS WEEK's requests for interviews.

**ON THE RISE:** New company headquarters nearing completion in downtown Rochester





# After B&L's problems surfaced, Gill ordered managers to follow the most conservative practices possible

veral other managers also left around the same time. When problems came to light in 1994, McCluski says B&L, its auditors, Price Waterhouse, and the audit committee of the board reviewed the situation in Hong Kong. Their conclusion: the problems did not materially affect Bausch & Lomb's published financial statements."

Outside accounting experts say B&L probably could not be known if the Hong Kong unit was indeed using tricks such as fake invoices. But if they could not have known specifics, sources close to B&L contend that lax headquarters oversight shares in the blame. Happy with Chan's numbers, they say, Rochester paid little attention to how he produced them. The targets for 1993 "were too big for Southeast Asia," says one B&L source. "I tried to be conservative, to bring it up to headquarters." But headquarters, they say, simply told him they hadn't heard hard enough.

One way to gauge a company's culture is to examine how it assimilates an acquisition. What core values does it instill into a new unit? What kind of conduct is encouraged or frowned upon?

Take the case of Outlook Eyeglass Co., a big player in undersunglasses that B&L acquired in 1992. The money-losing company became a training ground for executives. McCluski, now B&L's CFO, was Outlook president from 1992 to early 1994. He was hired by James T. Horn, who in this year was sent to clean up Hong Kong. But in turning the company around, the two employed a variety of questionable methods. When a Red Ball day loomed and they were behind target, McCluski and Horn would simply ship some orders in advance, and hope to avoid early shipment penalties. At times, reps were told to offer incentives such as price cuts or extended credit to move up a shipment by a few days. Outlook also would ship goods early to all truckers to take their time.

McCluski says neither he nor Horn engaged in these practices. He says some goods were shipped early in the first few months, but only because of warehouse snafus. "We'd never internally ship before a customer's start date," he says. And he says salespeople never offered discounts to move up sales. But ENR WEEK's account was independently confirmed by different sources. If they are correct, Outlook, too, began bending the line of acceptable accounting practices. "It's questionable" if deliberate early shipments should count as sales, says Robert S. Kay, a professor of accounting at New York University's Stern School of Business. "If it's done deliberately on a widespread scale, it's wrong."

After the SEC investigation was launched early this year, B&L underwent a remarkable transformation. Gill and other top executives ordered the company to follow the most conservative practices possible. Insiders and customers say there's no more

**TRAINING GROUND:** B&L introduced its tactics to Outlook Eyewear, a unit acquired in 1992

quarter-end wheeling and dealing. Sunglass distributors are asked to have no more than three months' inventory in stock. Bonus policies have been changed to reflect broader, longer-term goals. B&L has also now shifted to global management of its product lines. Sales for the first half were up 8.5% to \$1 billion while earnings from continuing operations apart from one-time changes were down 10.3% to \$61.6 million.

B&L's board, too, has lit a fire under management. The audit committee met several times to review B&L's 1994 financial statements and insisted that controls be strengthened. "The board made it very clear that this type of behavior wasn't acceptable," says Kenneth L. Wolfe, chairman of Hershey Foods Corp. and head of B&L's audit committee. But he, too, sees 1993 as an isolated case. "Unfortunately, when you have operations scattered throughout the world, people do things they shouldn't," he says. "But I don't think there's a larger problem."

As for Gill, he seems to reserve little blame for himself. "It's generally accepted that day-to-day operations of a company are



overseen by the chief operating officer," he says. "I don't mean to pass the buck, but... as chairman I'd have only a general understanding of what happened." Gill also professes astonishment that any B&L exec could have gotten the message that ethics should take a backseat to numerical goals. "I have no idea" why people would believe that, he says. "We think we are the most honorable beings on the face of the earth."

Corporate ethics specialists suggest Gill's explanation may be less than complete. Blaming individuals for multiple ethical lapses "is typical of companies that are well into denial," says Warren Bennis, chairman of the Leadership Institute at the University of Southern California's business school and the author of several books on corporate leadership. "They see no pattern despite the accumulation [of events]. A few bad people become scapegoats for the system."

A sharp dissonance between the message that senior executives believe they're sending out and the message heard by those down the line is also typical of companies with eth-



ical problems, say ethics specialists. The CEO "may believe he's telling them not to get into trouble," says USC's Bennis. "But if all the verbal and nonverbal signs sent out focus on making the numbers, he's giving them license to do unethical things."

## Cover Story

Chan—the two division heads held most directly responsible—were not punished. And the two men in charge of bringing B&L's questionable methods to Outlook have been promoted and put in charge of cleaning up. "It blows my mind," says a current sales manager at B&L. "If it's so important now that

Real questions remain as to how deep the changes at B&L go. Even Johnson and

we cross the i's and dot the t's, what happened to the people who were doing all this before?"

As for Dan Gill, he still sits in the chairman's office in Rochester, awaiting a move to his sparkling new headquarters. One former executive remembers a videotape presentation featuring Gill that was sent out to remote locations after the SEC investigation and B&L's disastrous 1994 results were announced. In the video, this executive recalls, Gill blamed the problems on poor decisions by individual division presidents and said the divisions needed closer monitoring. "It was like slapping the hands of children," says this executive. "when they were really acting on Daddy's orders."

*With Joyce Barnathan in Hong Kong*

## MONEY-LAUNDERING IN MIAMI?

**B**ack in 1985, Bausch & Lomb executives noticed that many of their distributors in Miami and New York were selling to Latin American customers. So B&L set up Lamex, a new Latin American export unit near the Miami airport. It became one of the company's fastest-growing divisions: By 1990, sales hit nearly \$25 million.

But many of the Miami deals were highly unusual. Latin American and Caribbean customers would arrive with up to \$50,000 in cash to pay for Ray-Ban sunglasses, according to more than a half-dozen former executives. The unorthodox sales added up: In 1990, according to internal B&L documents reviewed by *BUSINESS WEEK*, Lamex received \$5.6 million—23% of its total sales—in cash, cash equivalents, and third-party checks. Former executives say the cash transactions were well known at B&L. "The auditors would come in and see cash lying on the table and ask, 'What's that?'" says Armando Perez-Gili, a former Ray-Ban sales manager. "I'd say, 'One of our customers just paid us.'" A higher-level former manager in Rochester, N. Y., recalls questions being raised at headquarters in 1988, but nobody stopped the flow. "There was an urgency to meet the numbers," he says.

**SWIFT JUSTICE?** Of course, there's nothing illegal about accepting cash; stiff exchange controls and high tariffs mean many Latin Americans pay cash in Miami. But federal officials say tiny warehouse operators account for most of this trade. Multinationals deal in it only rarely. "There's a reason that people are paying a lot of cash," says one Internal Revenue Service investigator. "It's an indication customers could be purchasing [with] narcotics currency."

B&L declined to discuss Lamex,

saying in a written statement that "in an organization the size of Bausch & Lomb, there will be occasions when violations of company policy will be discovered, and we will deal with them swiftly and appropriately." But former managers say B&L's Miami shop took an even more dubious form of payment: checks drawn on third-party bank accounts made payable to someone else, and then endorsed over to B&L. Federal officials say such checks were commonly used to launder drug money in the late 1980s and early 1990s. Colombian money-exchange houses were used as go-betweens to launder funds for drug lords, who would provide dollar checks to the exchange houses. Although unfamiliar with the specifics of the B&L transactions and not commenting on them, Wilmer Parker, chief of the drug division in the At-

Lamex' general manager, Anthony Brea, and his controller resigned. Brea admits he diverted lenses through Canada, but says reports of other irregularities are "totally incorrect."

**HIT THE TARGET.** A new management team installed by Rochester spent two months combing through records. One key issue that the new managers never resolved: Did Brea follow rules requiring businesses accepting more than \$10,000 in cash in a transaction to file with the IRS? Brea swears that "in that area, B&L was very strict. We followed all the guidelines." But other ex-managers say the IRS forms weren't filled out until late in Brea's tenure. The new managers told buyers that "if they wanted to pay cash, they needed to follow proper procedures," says one. "We didn't see them again."

After the cleanup, the new man-

**According to internal documents at B&L, the company's Miami unit received 23% of its 1990 sales in cash or third-party checks**

lanta U.S. Attorney's office, says generally: "If a company was accepting third-party checks not payable to itself, either they were doing so with a blind eye to whether they were aiding and abetting money-laundering, or they were doing it with knowledge of what they were doing."

If B&L headquarters didn't seem to care much about Lamex' customers, executives in Rochester worried about another issue. After getting wind that the Lamex division might have been diverting goods back into the U.S. market did headquarters order a thorough audit. Insiders say they uncovered significant irregularities, and

agement team presented a report on the Miami operations to top corporate management in late 1991. They claimed that, of \$24.6 million sales in 1990, just \$13 million was legitimate. The rest went to questionable customers or products that were diverted back into the U.S. or Europe. Nevertheless, B&L headquarters insisted they boost 1991 sales above the prior year's. Says one high-ranking former manager: "We were told 'The shareholders don't care where the revenues were coming from before. You have to make it up.'"

*By Mark Maremont in Boston with Gail DeGeorge in Miami*



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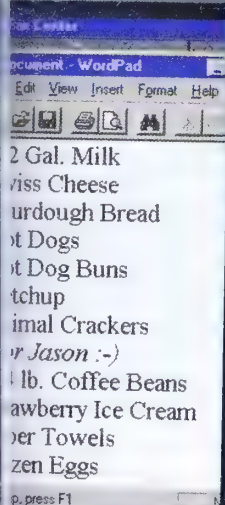
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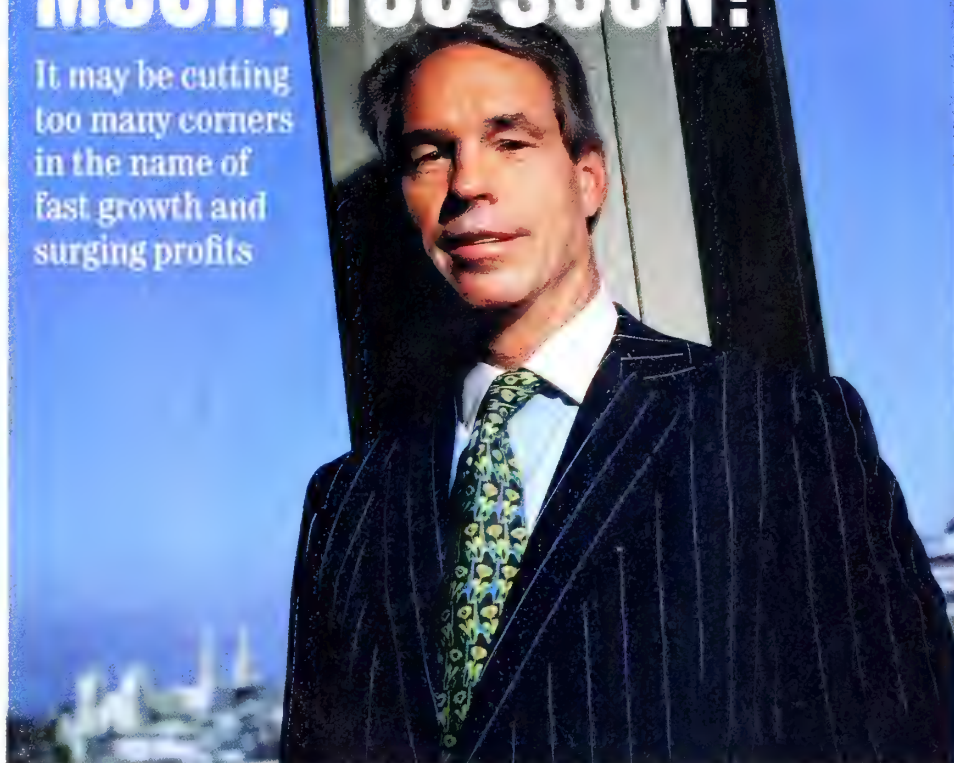
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SECURITIES FIRMS

# MONTGOMERY: TOO MUCH, TOO SOON?

It may be cutting too many corners in the name of fast growth and surging profits



**F**or Montgomery Securities, the 1990s have been the gold rush years. The 25-year-old San Francisco investment bank, which caters to growth companies often too small for the big Wall Street firms, is riding two of the major booms of the decade: the surge in initial public offerings and the explosion of the mutual-fund business. Its annual growth-stock conference, which attracted 1,000 brokers, managers, and other investment pros last month, has become the biggest such gathering since Michael Milken's Predators' Ball. The fast-moving, privately held firm, which at the turn of the decade had just \$100 million in revenue, expects to gross \$400 million this year—and is shooting for \$1 billion by 2000.

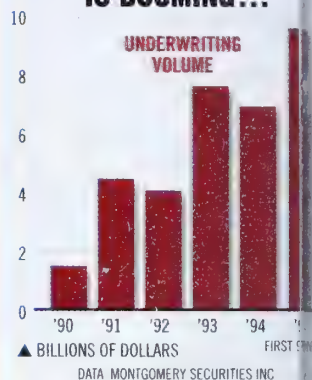
Thomas W. Weisel, 54, the CEO, chairman, and founder, as well as a competitive cyclist and avid art collector, is delighted to flout the securities industry's East Coast bias. "You don't have to go to New York to get a financial adviser, an underwriter or an institutional bro-

**WEISEL:** "Due diligence is not going to tell you what the future holds"

ker," he says. His lofty goal for the one-time boutique firm is to surpass in size three of the six major "bulge bracket" firms that do the lion's share of investment banking.

**VOLUME DEALING.** But as Montgomery reaches for such dramatic growth, questions are arising about whether it is taking shortcuts, sacrificing quality deals for quantity, and alienating customers in the process. A prime case is its initial public offerings business. The firm has been the lead underwriter for such superstars as Lone Star Steakhouse & Saloon, StrataCom, and Sunglass Hut. And it has downplayed volatile technology stock deals, which account for only 20% of its offerings. But the firm's average IPO return since 1990 is 68%, fourth place behind rivals Morgan Stanley Group, Alex. Brown & Sons, and William Blair. That's only a little better than the 63.5% return of the Standard &

## INVESTMENT BANKING IS BOOMING...



## ...BUT ITS IPO RECORD IS SO-SO

Average performance of initial public offerings in the aftermarket, Jan. 1990, through Aug. 31, 1995

| Lead Manager          |     |
|-----------------------|-----|
| MORGAN STANLEY        | 12% |
| ALEX. BROWN & SONS    | 9%  |
| WILLIAM BLAIR         | 7%  |
| MONTGOMERY SECURITIES | 6%  |
| PRUDENTIAL SECURITIES | 6%  |
| GOLDMAN SACHS         | 5%  |
| HAMBRECHT & QUIST     | 5%  |
| LEHMAN BROS.          | 5%  |
| ROBERTSON STEPHENS    | 4%  |
| MERRILL LYNCH & CO.   | 4%  |

DATA: SECURITIES DATA CO.

Poor's 500-stock index during this period.

Montgomery is also a target of at least six class actions, most involving IPOs. They charge that the firm omitted or misrepresented material facts, usually in prospectuses. Three cases have been settled for more than \$7 million plus stock and warrants, according to the newsletter *Securities Class Action Alert*. While declining comment on particular deals, Weisel says his firm shouldn't be held liable when clients liberally covered up bad news. A recent U.S. Court of Appeals ruling in request to overturn summary judgment involving a stock offering by Softa Toolworks Inc., underwritten by Montgomery and PaineWebber, said it was reasonable inference... that the Underwriters knew, or should have known, this fraud."

There are also questions about Montgomery's five-year-old and rapidly expanding mutual-fund group. While some of its funds have been hot, the group's performance has been mixed, especially



s year. According to Lipper Analytical Services, only two of the firm's 14 funds ranked in the top 20% in total return from Dec. 31, 1994 through Oct. 1995.

Some attendees at this year's growth conference complained that too many Montgomery underwriting clients were on the program. They were particularly outraged by client Hollywood Entertainment Corp., a Beaverton (Ore.) rental company. Its stock reached a new high of 34 on Sept. 19, the very day CEO Mark J. Wattles told attendees it was comfortable with Wall Street's \$5 earnings forecast of 54¢ a share.

**DOWN AND CRASH.** But on Sept. 28, the stock plunged nearly \$6. Minutes after market closed, Hollywood Entertainment reported that third-quarter revenues would be 7% below expectations,

that same-store sales would be down 3% to 4%. The stock dropped another 6 points the next day. It closed at 23½ on Sept. 21. Hollywood Entertainment did not recall seeking commitment. Says one New York money manager: "It's why I don't go to Montgomery conferences anymore. Their stocks run up and crash." Weisel vigorously rebuffed these criticisms. He says that only half the companies on the conference program are investment-banking clients. As Hollywood Entertainment, he says Montgomery encourages clients to disclose bad news quickly and that the firm's due diligence is exhaustive. But he argues in dealing with young companies, most thorough due diligence is not enough to tell you what the future holds. Weisel insists that criticism of the company won't prevent its investment bank and institutional brokerage from at least doubling revenue in the next five years. He also has high hopes for the client business, which specializes in investing money for wealthy individuals, many of whom got that way by making their companies public via Montgomery.

Montgomery is going to reach \$1 billion by the turn of the century, Weisel says, going to need strong growth from its mutual-fund and institutional-account management business, which opened its only five years ago, now has \$6.5 billion in assets under management and annual revenue of \$46 million. Considerable cutthroat competition in asset

management, this performance, says fund consultant Geoffrey H. Bobroff, is "absolutely, tremendously successful."

The master of this growth is R. Stephen Doyle, a veteran Montgomery partner who is the unit's chairman and CEO. Rather than plunging into the mutual-fund business through the common but expensive route of acquisition, Doyle and Montgomery Asset Management President Mark B. Geist built one from scratch by hiring talented portfolio managers from other firms. Their first product, the Small Cap Fund, opened its doors in November, 1990, a lousy time for such stocks. But under Stuart O. Roberts, hired away from Founders Funds, Small Cap took off when the market soared in 1991. The fund was up a spectacular 99% that year, putting Montgomery on the mutual-fund map.

"We'll never be so right about the market again," Geist says. Indeed, the fund has not matched that performance since, though it has retained its \$207 million in assets under management.

Montgomery Asset Management scored a similar hit with its \$1 billion Emerging Markets Fund. It was launched in 1992, before most investors even heard of "emerging markets" or Third World investing. Then, in 1993, came emerging-markets mania. The fund's 59% return that year contributed to Montgomery's reputation

as a hot fund company. Its Growth Fund scored only 21% in 1994, its first full year, but that was 23 percentage points better than the average fund.

Many of Montgomery's other funds, though, have been lukewarm recently (table). Still, Doyle has made strides in recruiting highly regarded portfolio managers from other fund groups. The lure: Portfolio managers get an equity partnership in the firm. And they are compensated according to revenue growth generated by their funds, not performance.

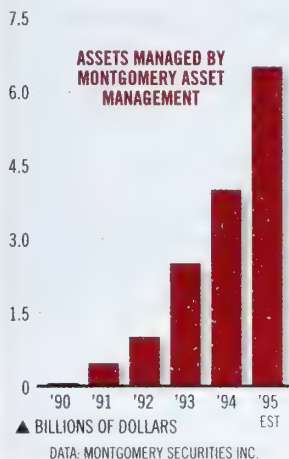
**"TECHNICAL VIOLATIONS."** One of those recruits, Roger W. Honour, who now runs the Growth Fund, was recently fined and censured by the Securities & Exchange Commission for trades at his former firms. Doyle says he knew of Honour's transgressions when he hired him but was unaware of the SEC investigation. He was charged with willful violation of antifraud laws in 25 stock trades. Doyle says he took "the view that those were technical violations. The SEC took a different view."

To achieve the kind of growth Weisel is expecting, Montgomery Asset Management will need new distribution channels for the funds. Close to 30% of fund sales come through Charles Schwab & Co. Right now, Montgomery sells funds without a commission, or "no-load," unusual for a securities firm.

With its plans for aggressive expansion, will Montgomery itself be on the IPO roster anytime soon? Not with finance company multiples so low and plenty of cash in the bank, says Weisel. With all the growth he is expecting, no wonder he's holding tight to his stake.

*By Nanette Byrnes in San Francisco*

## MANAGED ASSETS ARE ROCKETING...



## BUT MUTUAL-FUND RETURNS ARE MIXED

|                                      | Total Return* |             |
|--------------------------------------|---------------|-------------|
|                                      | 1995          | 1994        |
| <b>U.S. FUNDS</b>                    |               |             |
| GROWTH                               | 21.3%         | 20.9%       |
| MICRO CAP                            | 24.8          | NA          |
| SMALL CAP                            | 29.4          | -10.0       |
| EQUITY-INCOME                        | 24.0          | NA          |
| <b>U.S. DIVERSIFIED EQUITY FUNDS</b> | <b>27.1</b>   | <b>-1.7</b> |
| <b>INTERNATIONAL FUNDS</b>           |               |             |
| EMERGING MARKETS                     | -5.8          | -7.7        |
| GLOBAL COMMUNICATIONS                | 22.5          | -13.4       |
| INSTIT. EMERGING MARKETS             | -5.0          | -9.3        |
| INTERNATIONAL SMALL CAP              | 9.3           | -13.3       |
| GLOBAL OPPORTUNITY                   | 13.7          | -8.6        |
| <b>INTERNATIONAL EQUITY FUNDS</b>    | <b>7.7</b>    | <b>-3.3</b> |

\*Appreciation plus reinvestment of dividends and capital gains, before taxes. 1995 returns through Sept. 29

DATA: MORNINGSTAR INC.

## DOYLE LED ASSET MANAGEMENT'S GROWTH





## INVESTING

# ASK CHASE IF HE'S A 'PASSIVE' INVESTOR

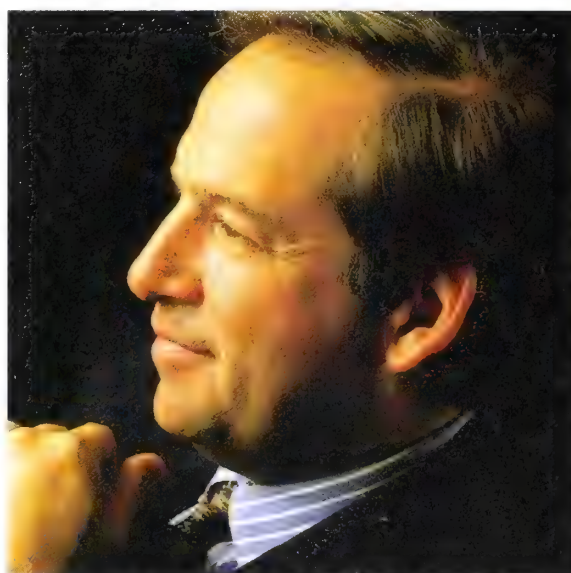
Suddenly, all eyes are on fund manager Mike Price

**S**hort Hills, N.J., is the kind of place to which Wall Street potentates retire for the night. But now, it's a place the smart money watches during the day as well. Mutual-fund manager Michael F. Price, who used a 6.1% stake in Chase Manhattan Corp. to prod it into a merger with Chemical Banking Corp., works out of a Short Hills office. Price scored a \$315 million unrealized gain on Chase and \$55 million on Chemical—and the Street wants to know the next target in Price's sights.

Price laughs at the idea of a hit list and doesn't see himself as a corporate raider. "We don't come to work looking for the next target," says Price. "We come to work looking to buy undervalued stocks. Sure, we were active in Chase, but there's over 300 companies here, and they're passive investments."

**MAJOR LEAGUES.** Price, 44, is one successful guy. The Mutual Series funds—Shares, Qualified, Beacon, and Discovery—total \$13 billion in assets. He makes money through traditional equity investing but also, on occasion, with illiquid investments that most funds shun. The funds plan to buy a 22.5% stake in Canary Wharf, the once bankrupt London office complex. Bankers say that will cost the funds \$150 million. Co-investors are big-leaguers: Laurence Tisch, Edmond Safra, Paul Reichmann, and Saudi Prince Alwaleed bin Talal bin Abdulaziz Al Saud.

Price has been jousting with managers and boards for years. Since May, he has been trying to force a sale of Bay View Capital Corp., a San Francisco thrift. Last year, he considered running an opposition slate of directors for the board of



**PRICE:** "We don't come to work looking for the next target"

Michigan National Corp.; management relented and agreed to sell to another bank. But pressuring a second-tier regional bank is one thing; challenging the "Rockefeller bank" is quite another.

Now, his once small band of followers has become a crowd, generating frequent rumors. One recently had Price, whose funds held 1.7 million Chrysler Corp. shares at the end of June, buying more to join Kirk Kerkorian's campaign against the auto maker. Price says he has unloaded Chrysler because "it's no longer cheap" and now believes Volvo is the world's cheapest auto stock.

Price's fund group is as unusual as its manager. Mutual Shares, Qualified, and

Beacon are near-clones of one another. There are no bond, money-market, or international funds—though the new fund, \$1.2 billion Mutual Discovery, has 40% of its assets in Europe. Price sees many European companies sell for high the price-earnings ratio they would command in the U.S.

A major portion of each fund is devoted to "value" investing, buying cheap stocks selling for a fraction of their true worth. Indeed, it's the ability to identify

cheap stocks that is at the heart of Price's success. Of course, investors can find them elsewhere.

But Price also blends in bankrupt investing and risk arbitrage, things rarely found in mutual funds. He learned the bankruptcy angle—where the investor as creditor takes an active role in molding a deal—from Max Heine, who founded Mutual Shares in 1949 and was active until his death in 1981. Price's funds have some \$1 billion in bankruptcies. Risk

arbitrage, investing in mergers and takeovers, accounts for \$700 million.

**"WEIRD MIX."** Bankruptcy and risk arbitrage have cycles of their own that do not correlate with the market. As a result, adding these investment styles to the funds gives them a low-risk profile compared with the Standard & Poor's 500 stock index. The largest fund, \$5.1 billion Mutual Shares, is only about 70% as volatile as the market. "It's a weird mix," says Ken Gregory, editor of the *No-Load Fund Analyst*, "but over time it generates excellent returns."

Price's funds have lagged the S&P the first nine months of 1995 (table). In part, that's because the funds have 20% in cash and have few high-octane tech stocks. But in 1994, when the average fund was down 1%, Price's funds had positive returns and beat the market. The funds have handily beaten the market averages over longer periods.

Price admits it's getting tougher to invest \$13 billion. Cheap stocks are getting scarce. So are bankruptcies. That's why he's bullish on Europe and will soon open a London office. It's also an admission that sometimes you have to get out of the limelight of Short Hills.

By Jeffrey M. Laderman  
in Short Hills, N.J.

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Ivax

United Healthcare

Sprint

ITT

Phillips

RJR Nabisco

Finova

Volvo

Sears Roebuck

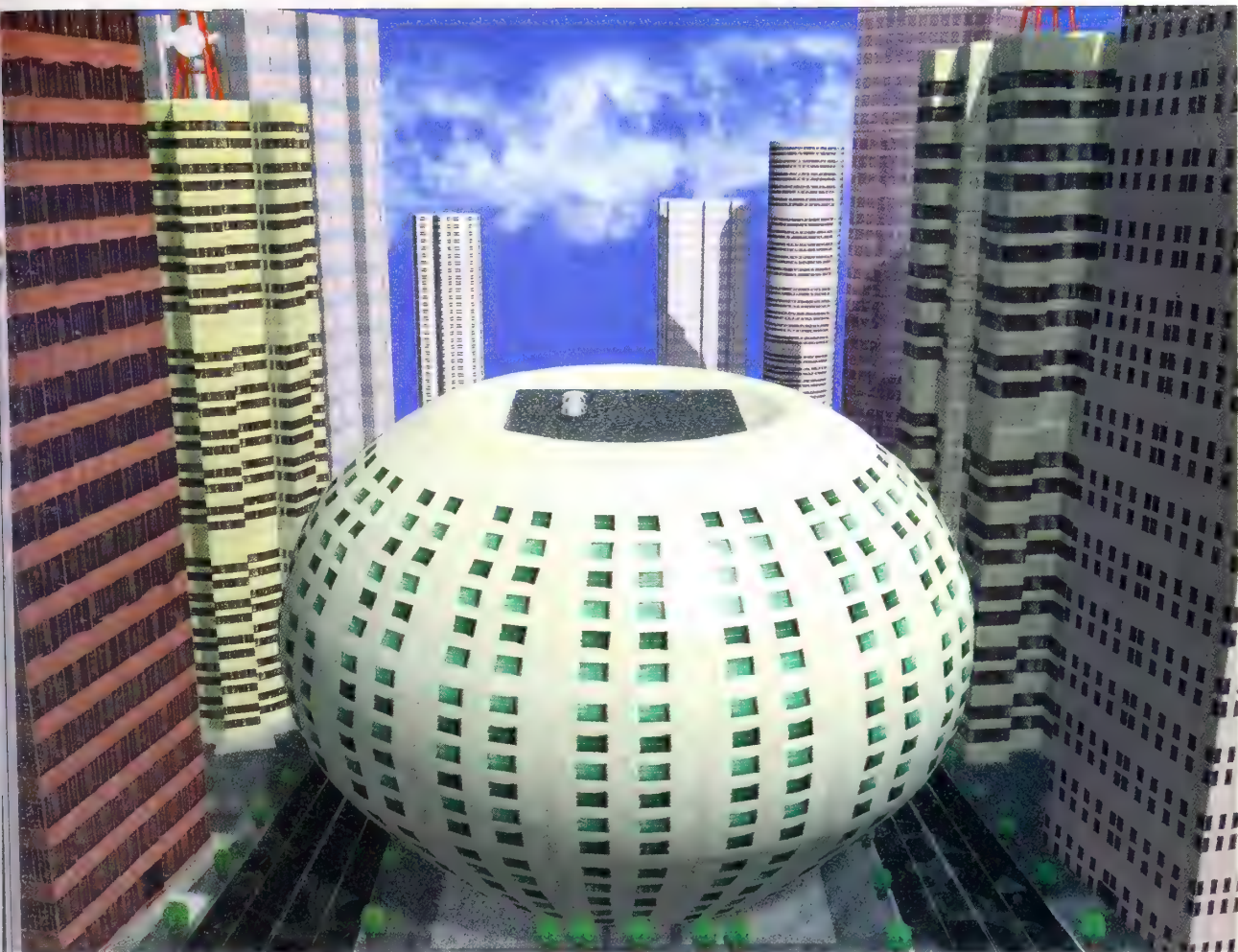
DATA: MUTUAL SHARES

## THE PRICE RECORD

|                  | TOTAL RETURN* |       |       |       |
|------------------|---------------|-------|-------|-------|
|                  | YEAR-TO-DATE  | 1-YR. | 3-YR. | 5-YR. |
| MUTUAL SHARES    | 27.0%         | 25.4% | 20.2% | 20.1% |
| MUTUAL QUALIFIED | 24.7          | 23.1  | 20.5  | 19.9  |
| MUTUAL BEACON    | 23.4          | 20.6  | 19.9  | 18.5  |
| MUTUAL DISCOVERY | 25.9          | 21.8  | NA    | NA    |
| S&P 500          | 29.7          | 30.3  | 14.9  | 17.2  |

\*Appreciation plus reinvestment of dividends and capital gains, before taxes. Three- and five-year returns are annualized averages. Returns for all periods are through Sept. 29.  
DATA: MORNINGSTAR INC





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the nine people I had to get drafts of my document to? Two on my floor. Three

floors you'd be embarrassed to take the elevator to. And four not even in this office

# How I walked four miles in a 9,000 square foot office.

And then I had to get each draft back with comments, and incorporate the

comments into my document by the following morning. So I basically faxed a

copied and delivered and then typed and re-typed

and re-faxed and re-copied and re-delivered



until my feet hurt and my legs were tired and I was sitting there starting

wonder why the heck running shoes aren't considered standard business attire

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CURRENCY

# THE MUSCLE-BOUND FRANC IS MAULING SWISS BUSINESS

Jitters over monetary union push the currency painfully high

**T**hrough 180 years and two world wars, the Swiss have benefited from their prized neutrality: no European Union for them. Yet now that the stakes are monetary, not military, the Swiss are paying a price for their independence.

The irony is dangerous to Switzerland's economic health. As the 1999 deadline for a single European currency approaches, jittery traders hang on every word about the criteria and timetable for monetary union. Terrified that the rock-solid German mark could suffer from being melded into the currencies of less stable countries, investors are pouring into Swiss francs. That's a new twist: Although dumping French francs or lire for Swiss francs is a time-honored practice, dumping marks just isn't done.

**BULGING SUITCASES.** The Swiss dearly wish this foreign money would go back home. Already up 12% this year against the currencies of Switzerland's main trading partners, the strong franc is pinching exporters and slamming tourism. Economic growth for 1995 is expected to be only 1.3%, down from the 2.4% originally forecast.

Bankers say that international money managers and corporate treasurers are shunning German bonds for Swiss ones to hedge their portfolios, and private savers are driving across the border with their savings packed into suitcases.

"The Swiss market is just too small to take it all," says Peter Buomberger, chief economist at UBS in Zurich.

The currency pressure is speeding up the restructuring that Swiss companies began in the early 1990s when they were gripped in recession along with the rest of Europe. Now, even more companies are likely to begin outsourcing supplies and moving production abroad. Elevator maker Schindler, for example, plans to close a component plant in Switzerland and one in Germany, shifting production to Spain. The company is under so much pressure that Crédit Suisse forecasts profits may be slashed in half. Coupled with cheaper Asian and Central European competition, the currency squeeze leaves little room for profits. "We have a choice: Either we give up our margins or we lose our business," says Bruno Allmendinger, treasurer of Sulzer Ltd., a machine-tool maker whose profits slipped 29% in the first half. Watchmaker Swatch won't raise prices—but expects flat profits as a result.

Currency translation is crimping results even at Switzerland's blue-chip multinationals. Drugmaker Ciba-Geigy

**SELLING SWATCHES:** The company CEO vows not to raise prices

gets 93% of its sales outside Switzerland. So while net profit in the first half soared 37% when measured in local currencies, it posted a mere 5.9% gain in Swiss francs. Consumers are also buying at higher prices from Nestlé—although, on top of the currency effect, suffering from rising costs for raw materials. In foreign-currency terms, Nestlé sales climbed 10% in the first half. In Swiss francs, they slumped 1.5%.

**"SCARY."** To dampen the exchange-rate losses, more companies are trying to avoid paying in francs for supplies. Swissair buys fuel and handles aircraft leasing in dollars: It handles reservations from operators in Bombay and plans to do more aircraft repair in the United States and Belgium. But the real pain comes from high-volume ticket sales in Italy and France, where softer currencies hurt Swissair's margins.

At home, families in Geneva drive to France to do their grocery shopping. Border towns such as Lugano are deserted as vacationers skip to Italy. Tourism, which accounts for 6% of Switzerland's gross national product, suffered its worst August in 43 years. And the strong franc's effect on the economy comes on top of anemic consumer spending. "It's getting to be a scary situation," warns Hans Kaufmann, chief economist at Bank Julius Baer & Co.

Swiss authorities have few options. A half-point cut in the discount rate on Sept. 21, to 2%, had little effect—Swiss

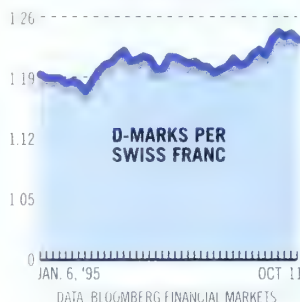
rates were already the lowest in Europe. Perhaps in 12 to 18 months, low rates will put the economy back on track with higher domestic investment and consumption. But until the political matter of European monetary union is settled—which could take at least five years—Swiss franc will remain volatile. Says Martin Rösigen, European

securities analyst for Morgan Stanley & Co. in London: "That's ample time for unpleasant surprises."

While the debate over monetary union grinds on, notes Kaufmann of Julius Baer, Switzerland could try to cool the market by reconsidering membership in the EU. This time, a little touch of neutrality may be worth it.

By Karen Lowry Miller in Basel  
with John Parry in Geneva

## RIDING HIGH





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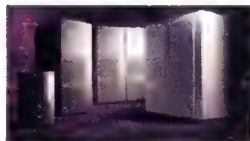
# Oracle's Larry Ellison on AT&T WorldMark Servers

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BY GENE G. MARCIAL

## A STIFF BROOM GOES AFTER PIER 1

When value investor Mark Boyar finds a compelling stock, he usually cleans up. He was among the first to pressure Sears Roebuck, Hilton Hotels, and U.S. Shoe to maximize shareholder value by breaking up assets or selling out. Sears spun off some units, Hilton Hotels split up, and U.S. Shoe agreed to be acquired by Luxottica. What's Boyar targeting now?

He reckons Pier 1 Imports (PIR), the nation's largest retailer of imported home furnishings and related items, is worth much more than its current 10% a share. Pier 1 operates 645 stores in 47 states, Britain, Canada, and Mexico.

Boyar, who has accumulated some 350,000 shares, told Chairman Clark Johnson in a recent letter that he was among the "frustrated" shareholders hoping management would act to boost the "underperforming" stock. It has traded between 7 and 10% all year. From 1988 to 1994, says Boyar, the stock trailed its peers and the Standard & Poor's 500-stock index. Although revenues have climbed to \$712 million, up from \$175 million five years ago, earnings have been lackluster.

### TOO LONG IN A RUT



"Pier 1 should get higher returns on sales, and the stock deserves a higher price," insists Boyar. One factor turning off investors, he says, is the company's shareholder rights, or poison pill, aimed at thwarting takeover bids. And Boyar cites the "very generous bonus incentive plans" offered to top brass "in spite of sluggish performance."

Boyar also denounces management's \$3 million investment in a limited partnership—run by a board member's

brother—that invests in small- and medium-capitalization stocks. Boyar thinks the money should be used for operations or for buying back its shares. There's "no justification" for such investment, he says. The company disclosed the \$3 million investment in a public document.

Pier 1's reaction? "The response was horrible," says Boyar. Johnson said that using \$3 million of the company's cash hoard of \$30 million was justified and is earning good returns. He also defended the poison pill as a sound defense measure. Johnson disputed Boyar's claim that the stock has been a laggard, noting it's close to its 23-month high of 12%.

"By all benchmarks, however, the stock is cheap," argues Boyar, who figures it's worth 14 as is. And if management takes the right steps, he's convinced that it will hit 20 in two years. Johnson sees strong Christmas sales and expects record results this year before certain extraordinary charges.

## AMERICA ONLINE: HAS IT PEAKED?

America Online (AMER) has been one of the Street's hot stocks this year. At 61, AOL has a market cap of nearly \$4 billion and trades at a monumental 70 times estimated 1996 earnings. But watch out. AOL may have peaked at 74½ in mid-August—and has slipped since. Some bears say there's more sliding ahead. They think the stock is headed down to the 20s within a year.

What went wrong at the No. 1 provider of online services? One hedge-fund manager who has been shorting the stock explains: "America Online, which has never been cash-flow positive and uses aggressive accounting in reporting its meager earnings, faces increasing competitive pressures."

The reason, he says, is that user fees, which have been declining, will drop further, as Microsoft, AT&T, and MCI Communications enter the online business. AOL, he warns, faces a big margin squeeze from content providers that may demand a bigger share of revenue. (AOL carries BUSINESS WEEK Online.)



BOYAR: Pier 1 is "undermanaged"

He predicts that such providers will move from restrictive closed networks such as AOL, to the Internet, where they can have their own home page, receive 100% of the revenue, and control the look and feel of products. He notes that CompuServe, a large competitor, has cut prices and Microsoft has started marketing its own network at lower prices. DataQuest, a consulting firm, predicts rapid growth in online service but sees slow growth in revenues due to anticipated price erosion.

Jeff Gorman at Cowen & Co. says in an internal memo that the stock does not reflect future uncertainties. While AOL could still expand its subscriber list, he warns that the "cost is increased customer churn, margin erosion, and [less] profitability."

## TAKING WING WITH KELLSTROM

When Zivi Nedivi took over in August as president of Kellstrom Industries (KELL), he did something unusual for a chief: He bought \$1 million worth of stock at market price—5½¢ a share. Since he was going to run Kellstrom, explains Nedivi, he knew the shares were a bargain. Indeed, he knows the company well: Nedivi owned it when it was a private outfit known as Rada Electronic Industries, an Israeli avionics-systems maker.

Kellstrom now buys, refurbishes, and resells parts for commercial-jet engines. Customers include Northwest Airlines, TWA, El Al, and various engine makers and parts distributors. So far, business has been brisk, thanks to the world's aging aircraft and a shift by many airlines toward keeping a very lean inventory of spare parts.

Kellstrom helps customers reduce engine-maintenance costs by providing competitively priced engine parts. The company "leads the market in quality assurance," says Anthony Stoss, an analyst at GKN Securities. He sees revenues jumping to \$22 million in 1996, up from an estimated \$14 million this year. He expects Kellstrom to earn \$1.3 million, or 31¢ a share (fully diluted) this year and \$2.3 million, or 44¢ next year. It earned \$736,000, or 27¢, last year. Chairman Yoam Stern thinks these estimates may prove conservative. David Jordon of J. W. Charles Securities thinks the stock is cheap: "With its fast growth and planned acquisitions, the stock will at least double in a year," he says.



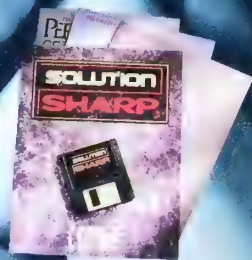
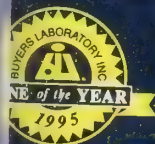
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## SOFTWARE

# LOOKING FOR THE NEXT NETSCAPE

Internet startups are drawing a swarm of investors

**A**ug. 9, 1995, is a date investors are not likely to forget. That is the day Netscape Communications Corp., a maker of Internet software, went public. Netscape's stock, offered at \$28 a share, soared to nearly \$75 before ending its first trading day at a less stratospheric \$58, making multimillionaires of its founders and insiders.

Investors weren't the only ones to take notice. So did scores of entrepreneurial-minded programmers, software executives, and computer-science students dreaming of creating the Next Big Thing. No one knows what that will be—or even if Netscape, now trading around \$60, will live up to the hype. But investors will have plenty of opportunities to bet on Internet plays. The Internet “is the first thing I’ve seen that resembles the PC when it hit its sweet spot,” says Rob Glaser, who worked for Microsoft Corp. in the early 1980s and is now chief executive of Progressive Networks, a Seattle-based startup that makes software for delivering audio over the Net.

**EARLY BIRDS.** Despite periodic sell-offs of technology stocks—such as the one that hit the market Oct. 9—the Internet phenomenon remains an investment opportunity. Sales of software for the World Wide Web are expected to swell from \$260 million this year to \$4 billion in 1996, according to Hambrecht & Quist Inc. There's a need for all sorts of programs, including “tools”



**Exults an investor: “The startups that are here today will own the market tomorrow.” Maybe—if they’re still alive**

for setting up Web servers, packages to scour the Net for information, and technology to make the Net safe for business. That adds up to the hottest climate for startups the software industry has seen in a decade. “This is one of those rare, gigantic revolutions,” says Charles Fer-

guson, chairman of Vermeer Technologies Inc., a Cambridge (Mass.) software startup that makes Web publishing programs.

Hundreds of companies are seen their fortunes in cyberspace—names like InfoSeek, First Floor, and Yahoo. Some started out with the Internet in mind, others stumbled onto it but all see the sprawling Web as a ticket to success. And with the market developing so rapidly, “the startups here today will own the market tomorrow,” says Ann Winblad,

founder of Hummer Venture Partners in Emoryville, Calif., who put \$1.9 million into an Alto (Calif.) startup Site Technologies Inc. in June.

Overall, venture-capital investment in Net-related companies will triple over last year's \$42 million, says David T. Gleba, president of VentureOne Corp., a researcher that tracks venture investments. In the first half, \$68 million poured into fledgling Internet companies, he reports.

Dozens of Internet startups may be in line for public stock offerings—if they don't get snapped up by established software makers and online-service providers are quickly gobbling up newcomers. America Online Inc. alone has bought up a half-dozen promising software startups in the past year, including the \$30 million acquisition of Web browser developer BookLink Technologies and the \$4 million purchase of Navisoft Inc., which makes program publishing on the Net. Netscape, flush with its Sept. 21 shelled \$109 million for Colombia Software Inc., a fledgling maker of document-sharing software. “It's a sea market,” says Yogesh Dalal, a partner with Mayfield Fund, a Silicon

Valley venture-capital outfit.

Just a year ago, the situation was far different. When Ferguson was looking for financing for Vermeer in late 1994, a major sell was required. “No one knew what the Web was,” says. “We were too far ahead of



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## Cooked up in a Mexican restaurant and developed in a garage, one idea has raised \$3 million

curve." Eventually, Ferguson lined up \$4 million from Matrix Partners, Sigma Partners, and Atlas Venture. Vermeer's products make it simpler for nontechnies to publish on the Net. Its first program, called FrontPage, walks developers through the process of creating a Web site. Vermeer is negotiating an additional \$6 million from its original partners and new investors. This time, Ferguson says, "we are totally surrounded" by potential investors.

The most successful Internet startups are pushing beyond the Web-browser market that Netscape dominates. Progressive Networks, for instance, has technology for delivering live audio feeds over the Internet, instead of using time-consuming downloads. The RealAudio software has made it practical for broadcasters, such as ABC and National Public Radio, to put their programs on the Net. ABC, for example, broadcast live coverage of the O.J. Simpson trial on its Internet site. Listeners also can click on programs they have recorded and listen at their convenience—fast-forwarding and re-winding or crafting custom playlists, too.

**SELLING ADS.** Progressive is off to a fast start. Over a half-million consumers have downloaded the free "player" program. And Microsoft is bundling the player with its browser for Windows 95. More than 100 Internet sites offer RealAudio sound clips, and Glaser says the company is well ahead of its goals for this year. Naturally, investors are knocking. However, Glaser says that for now, the company—which is privately financed by individuals, including Lotus Development Corp. founder Mitchell D. Kapur and various Microsoft millionaires—is saying no thank you.

As the amount of information on the Internet continues to mushroom, there's an exponentially expanding need for software to sift the clutter. So David Filo and Jerry Yang, two graduate students at Stanford University, found a

ready market for Yahoo, their savvy guide to cool Web sites. The pair quickly raised an estimated \$1 million from Sequoia Capital, and Yahoo Corp. was founded.

Programs for searching the Net are "the hot story of the moment," says Gene DeRose, president of market researcher Jupiter Communications Inc. One such startup is InfoSeek Corp., a Santa Clara (Calif.) company founded in January, 1994, by Steve T. Kirsch. He had also founded software maker

the idea of searching even further. The company was founded in 1993 by 25-year-old Joseph R. Kraus and five former Stanford University graduate students. Their idea: Instead of searching for specific keywords, why not search the Net for concepts? After hashing out their idea in a Mexican restaurant, the five started work developing a program in a Cupertino (Calif.) garage. In December, Architext raised \$3 million from Kleiner Perkins Caufield & Byers, Institutional Venture Partners, and some small investors.

Kraus prefers to think of Architext more broadly as a "media navigation" company. The company's first product, called Excite, was introduced on Oct. 1. The program uses sophisticated algorithms to conduct concept-based searches. Search on "intellectual property," for example, would include sites for documents involving patented topics such as software piracy that a keyword search would miss. Since the company has signed eight advertisers, including MCI Communications Corp. and AT&T, whose ads appear on the Architext search page.

**UNDAUNTED.** A bunch of startups see an opportunity in helping Corporate America blend in-house networks with the wheeling Internet. Spider wants to provide the software "glue" to connect corporate databases with information stored on Internet servers. And First Floor Inc. in Mountain View, Calif., makes Smart Files, a Lotus Notes groupware program for the Web.

The Internet is chock-full of opportunity. But so was the PC business a dozen years ago. For every Compaq, there were a dozen flameouts—Coho Data Products, Eagle Computer, Vector Graphics. "Everyone's hoping the next Netscape," says Architext's Kraus. "That's pretty unreasonable to expect." However, it won't stop from trying.

By Amy Cortese in New York  
Robert D. Hof in San Francisco

### Startup Fever

Software Entrepreneurs Look to the Net

| COMPANY                     | PRODUCT/DESCRIPTION                             | FUNDING                             |
|-----------------------------|-------------------------------------------------|-------------------------------------|
| <b>ARCHITEXT</b>            | Excite<br>Conceptual search program             | \$3 million<br>in venture capital   |
| <b>FIRST FLOOR</b>          | Smart Files<br>Net-based collaboration software | \$5 million<br>in venture capital   |
| <b>INFOSEEK</b>             | InfoSeek<br>Online search service               | \$6 million<br>in venture capital   |
| <b>PROGRESSIVE NETWORKS</b> | RealAudio<br>Brings audio to the Internet       | undisclosed<br>private investment   |
| <b>SPIDER TECHNOLOGIES</b>  | Spider<br>Links the Net to corporate data       | \$1.9 million<br>in venture capital |
| <b>VERMEER TECHNOLOGIES</b> | FrontPage<br>Personal Web publishing tools      | \$4 million<br>in venture capital   |
| <b>YAHOO</b>                | Yahoo<br>Online guide to the Net                | \$1 million<br>(estimated)          |

DATA: BUSINESS WEEK, COMPANY REPORTS

Frame Technology Corp., recently acquired by Adobe Systems Inc.

Kirsch started out with the idea of providing a low-cost information retrieval service. It didn't take long for him to realize that the best delivery vehicle for his service was the Internet. His strategy: give away the search service and sell advertising to pay the bills. InfoSeek gets 1.5¢ per search from advertisers, and although the company has added a \$9.95 monthly subscription service, it still makes more money on the larger volume of "free" searches. Today, InfoSeek is one of the most popular search engines on the Net—mainly thanks to its prominent placement on Netscape's Internet site.

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## INFORMATION MANAGEMENT

# PUTTING A KEENER EDGE ON SABRE

The reservations giant moves to face down new online rivals

**Y**ou might expect AMR Corp., parent of American Airlines Inc., to be giddy over the Internet. After all, some industry experts predict that this vast, public computer network could save airlines billions of dollars in commissions by helping them sell tickets directly to individuals and corporations instead of through travel agencies.

The Net may indeed mean good things for American, but it could spell trouble for another AMR unit, the \$1.5 billion SABRE Group and its SABRE Travel Information Network, a computerized reservation system (CRS) that processes 44% of travel agents' airline bookings in the U.S. With operating margins of 24% last year, SABRE helped cushion AMR through the downturn in the airline business, where margins were just 4%. Besides serving airlines, SABRE also collects lucrative fees from car-rental companies, hotel chains, and other travel-service providers that use its system.

**FURIOUS POSITIONING.** The rise of new sales channels such as the Internet and commercial online services threatens to make SABRE's lock on the travel-agency business increasingly irrelevant. Analyst Julius Maldutis of Salomon Brothers Inc. says the Internet could cut the proportion of major airline tickets sold through agents from 90% to 40% in the next three years. "Travel agents are in a very unpleasant place in the food chain," agrees Andrew O. McKee, president of Adventure Media Inc., which helps tour



**CEO DURHAM:** Spending millions and forging alliances

operators sell via computer networks.

So SABRE is spending millions to better reach consumers directly—even as it continues investing in its traditional travel-agency business. It's revamping easySABRE, a decade-old system that reaches consumers via online services, and it plans to start selling tickets over the Internet next year. It's also trying to forge alliances with key players such as Microsoft Corp. and Time Warner Inc. "We think we understand better than most how consumers buy travel," says Michael J. Durham, chief executive of the SABRE Group since last March. "Thus we think we can do a better job of providing an electronic medium for them to do it." Once SABRE figures that out, it also must figure out how much it can

charge consumers and dream up other revenue sources to make up for the loss in agent fees.

No matter what, players old and new are furiously positioning themselves in a world of direct, electronic travel sales. With commissions and CRS fees eating up about 15¢ and 3¢, respectively, every travel dollar, some airlines and hotels are seeking alternatives. By early 1996, Southwest Airlines Co. and the Hotel Industry Switch Co. (THIS

company, owned by a consortium of hotel chains, each plan to start booking reservations themselves over the Internet. Meanwhile, Electronic Data Systems Corp., a computer-services giant, has taken a stake in System 1 Co., the U.S. marketing arm of Amadeus, a European CRS. And United Airlines Inc. has agreed to deal to put a link to its Apollo CRS on the Microsoft Network.

To stay competitive, SABRE must make its system easy to use by average consumers, not just agents trained in arcane codes. "The [CRSes] are technological dinosaurs," says Charles Zug, vice-president of interactive services at THG. Nicholas A. Athanasiou, a consultant at Arthur D. Little Inc., estimates SABRE will spend about \$120 million a year on new systems, far more than rival CRS companies. Yet, most of that will go to help travel agencies.

There's still the question of just how many masses of consumers will book their own seats. After a decade, easySABRE generates only 1% of SABRE's volume. That's a comfort for travel agents, but they see that a computer-savvy public won't rely on them forever for simple reservations and ticketing. Those who help companies control their travel spending and offer personalized consulting services will always have a role, insists Robert J. Funk, chief information officer at Rosenbluth International, Philadelphia, a big agency. That is, if somebody figures out how to do it on the World Wide Web, too.

By Wendy Zellner in Detroit

## New Options in the Air

New ways for travelers to tap into SABRE's reservation system.



**easySABRE** Twelve online networks, including America Online and Prodigy, offer access to SABRE's reservation system. Microsoft Network may be next.



**BUSINESS TRAVEL SOLUTIONS** New

software for PC networks may help corporations bypass travel agents and manage travel expenses better.



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DATA: AMR CORP.



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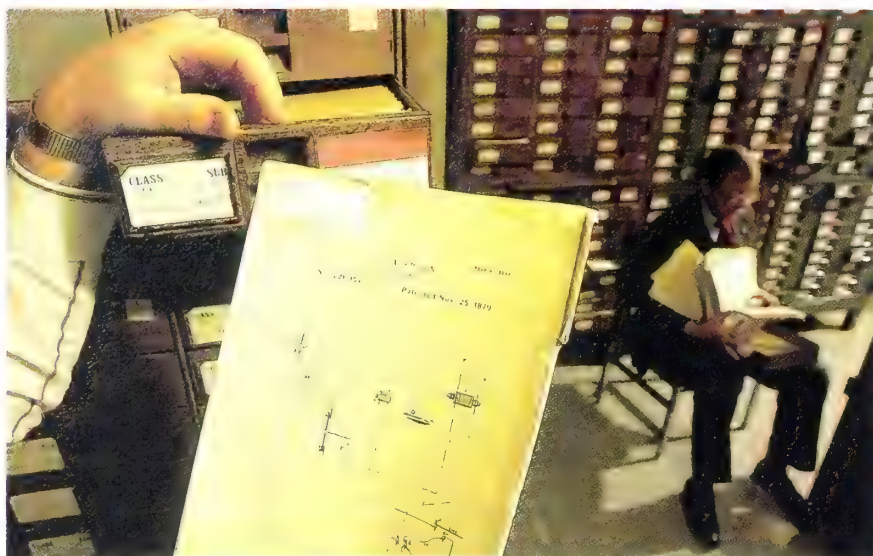
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## INTELLECTUAL PROPERTY

# NEW PATENT OFFICE PENDING

Pressure to reinvent invention central builds in Congress

**T**hink corporate reorganizations are tough? Try reengineering a 200-year-old federal institution staffed with 5,100 civil servants. That's the kind of challenge lawmakers and politicians took on when they drafted two bills this year that would convert the U.S. Patent & Trademark Office (PTO) into a semi-independent, government-owned corporation.

The idea has been around since 1989 but didn't take legislative form until last May, when Representative Carlos J. Moorhead (R-Calif.) introduced a bill to "corporatize" the PTO. Vice-President Al Gore answered with a plan modeled on Britain's "performance-based" system. Gore wants to create an Intellectual Property Organization headed by a CEO, half of whose pay would be pegged to productivity and other performance measures. In the current system, bonuses are tiny.

**SQUANDERED.** The two reform proposals spring from the same gripes. Unlike other government agencies, the PTO supports itself entirely from fees. But each year it turns over one-fifth of what it collects to Congress, which keeps part for its own pet projects. Last year, Congress' take was \$25 million. "A properly functioning government corporation

wouldn't have to endure such a raid," says Michael K. Kirk, executive director of the Arlington (Va.)-based American Intellectual Property Law Assn., which backs corporatization.

By chopping the PTO's bureaucratic fetters, Moorhead and others want to make the office more flexible and cut waste. Millions of dollars are squandered on inflated rents set by the General Services Administration. And even though the PTO generated \$542 million last year, it can't expand staff because of the 1994 Workforce Restructuring Act, which obliges the feds to shed 272,900 jobs.

Both corporatization bills would let the commissioner or CEO modernize facilities and upgrade staff. That's important because patent filings in difficult fields such as computer software are growing far more quickly than total

**TOO DRASTIC?** Critics fear that a "performance-based" agency would cater to corporate interests or rubber-stamp applications

applications, according to the *Intellectual Patent News Service* in Belmont, Mass. (chart). To speed processing and improve patent quality, the office needs to attract more highly educated examiners and equip them better.

Critics of corporatization, ranging from PTO staff to independent inventors and small business companies, say the plan is drastic and unnecessary. More than 300 examiners have sent letters to members of the House intellectual property subcommittee urging amendments to existing patent code instead of corporatization. "I fear that a CEO whose bonus is pegged to productivity might rubber-stamp applications or cater to large corporate customers."

**RED TAPE.** The bills' sponsors, along with PTO Commissioner Bruce A. Lehman, argue that oversight would prevent abuses. "The fears are 180 degrees wrong," says Lehman. "We want to provide better services to fee-payers."

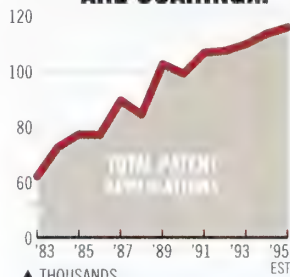
Independent inventors are hypersensitive to change, having lost skirmishes in which the U.S. adopted what they regard as weaker protections of the European and Japanese systems. Groups such as IBM, Motorola, and Intel have fought against independents in those cases, but may do so again if they decide that corporatization could cut red tape.

Some want America to become the fastest processor of patents in the world, says Michael Maize, Intel Corp.'s director of government affairs.

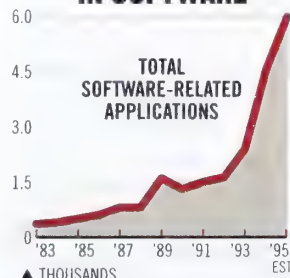
The PTO won't be revamped overnight. One thing, House Republicans seem determined to bundle the bill with legislation to abolish the Commerce Dept., which oversees the PTO—a plan President Clinton may be sure to veto. Eventually, corporatization seems a likely outcome since it has strong bipartisan support. In the fact is, a more flexible, responsive patent office could help bring innovations to market.

By Neil R. McMillen  
in New York

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DATA: INTERNET PATENT NEWS SERVICE



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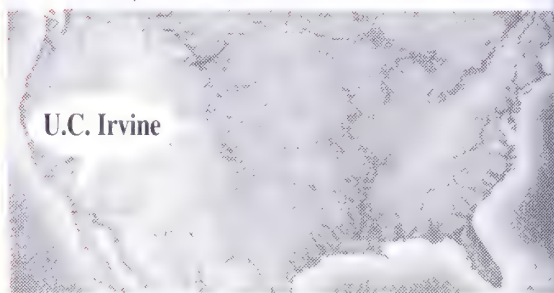
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PUTING

# THE NETWORK OF TOMORROW OR WHENEVER

is supposed to be faster. So why isn't it taking off?

Glenn Daly wants students at New York Medical College in Valhalla, N.Y., to probe the mysteries of the body with the help of digitized clips. Daly, the school's computer manager, realized last year that he had to rebuild the school's computer network to handle such capabilities as well as pressing needs like Internet access and the transmission of scanned-in documents. He decided to use a powerful new computer networking technology—ATM (asynchronous transfer mode), which promises a giant increase in speed and the ability to handle networked multi-media programs.

Despite the wide-spread impression—largely fueled by fanfare over network gear—that ATM is ready for action, Daly concluded it wasn't ready for him. And he wants to upgrade the network by next June, but won't wait any longer. He is leaning toward ATM in another type of network—fiber distributed interface—which will meet his needs for now. Daly: "I am not one of those network managers who are on the bleeding edge. I want to go with what we know works."

The question, ATM is the future. It promises the ability to squeeze video, and voice into a pipeline. What's more, ATM's high speed makes typical local-area networks (LANs) running Ethernet or Ring look downright catatonic. Companies that make ATM gear are anticipating the arrival of the ATM age and such early customers as Texas Instruments Inc., which uses ATM to carry

essential traffic among six of its locations.

For now, though, most network managers are browsing, not buying. For LANs—which carry the bulk of computer network traffic—ATM is expected to make up less than 0.4% of the 56 million

juiced-up LAN standard called Fast Ethernet, which has the additional advantage of working more easily with regular Ethernet. "Fast Ethernet is stealing ATM's thunder," says David Goodtree, a senior analyst at Forrester. ATM still has the edge in handling networked multimedia, but that's not a major need of most network managers. And several important features of the ATM standard remain up in the air.

**JACKRABBIT START.** The bottom line: Market forecasters who once thought ATM would be taking off about now have pushed back their projections. Forrester's Goodtree thinks it will penetrate wide-area networks around 1997 or 1998—and LANs sometime after 2000. That's bad news for dozens of suppliers

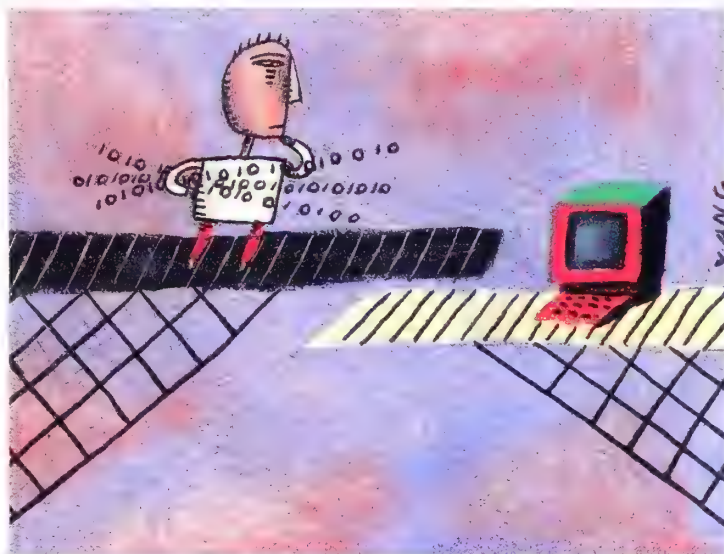
that have invested heavily in hopes of a quicker pay-off. Middlebury (Conn.)-based General DataComm Inc., whose stock went from under \$2 to almost \$36 in five years partly on hopes for its big ATM switches, has lost nearly two-thirds of its value since January.

The market for smaller gear that goes into office networks is especially crowded, with such companies as FORE Systems, Bay Networks, Newbridge Networks, and UB Networks all fighting it out. Ron Jeffries, a principal of Jeffries Research in Santa Maria, Calif., wrote last month in his ATM User newsletter: "I expect that life for most ATM switch vendors will be nasty, brutish, and short."

Work on hammering out an ATM standard got off to a jackrabbit start in the early 1990s, thanks to the ATM Forum, a nonprofit consortium of suppliers, service providers, and customers. But progress has slowed markedly as the forum has begun to tackle the tougher issues and as membership has passed the 700 mark. "The more people get involved,

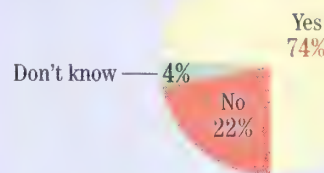
the longer the standards process takes," says Joe Skorupa, ATM marketing director at FORE Systems Inc. in Warrendale, Pa. "The only alternative is to have a benevolent dictatorship, and not everyone is willing to deal with that."

The forum claims most technical standards are complete, but that does



## ATM: Customers Are Browsing, Not Buying

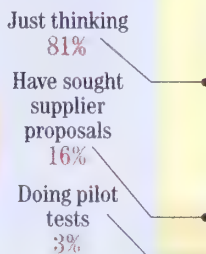
Is your company interested in deploying a wide-area network using asynchronous transfer mode?\*



DATA: FORRESTER RESEARCH INC.

\*QUESTION ASKED OF NETWORK PLANNERS AT 50 LARGE U.S. COMPANIES

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ports shipped this year, according to Dell'Oro Group in Menlo Park, Calif. Sales are only slightly stronger in wide-area networks, says Forrester Research Inc. of Cambridge, Mass.

Price is one big hindrance. Installing ATM in LANs costs about \$1,500 per personal computer, vs. \$300 or \$400 for a





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not mean different companies' equipment will work together smoothly. In a lot of cases, the standards are sufficiently vague that 10 vendors will claim compliance, and no 2 of them would work together," says Kevin Tolly, president of Tolly Group, a technology consulting and testing firm in Nasquan, N.J.

**SOFTWARE CATCH-22.** ATM suppliers even deliver yet on one of their promises—that ATM networks will handle voice along with video and data. As opposed to data, which can be sent in regularly timed chunks, voice requires a steady, unimpeded flow. While the theory of how to do that is well known, actually delivering good-quality voice at an acceptable price has so far stumped suppliers.

Demand for ATM won't take off until software that exploits its features is available—and software requires a market. "It's a chicken-and-egg problem," says R. Gary Byrd. Although Byrd is IBM's program manager of ATM market planning and a strong proponent of bringing ATM to the desktop, his

**Suppliers have yet to deliver on a key promise—that ATM will handle voice, too**

PC is connected to a Token Ring.

So, with full-scale adoption only some years off, many suppliers are offering ways to ease it into existing networks. The ATM Forum recently adopted a standard for connecting ATM with frame relay, a high-speed version of traditional packet switching, which breaks up data into bundles for "multiplexing" over networks. Some suppliers are promoting ATM as a technology that will support current networks through emulation. But that, too, is in its early stages of availability.

All those caveats don't trouble companies as Texas Instruments, Intel, Stearns, Tandem Computers, and others that are using ATM today. More common, though, are the likes of Michael Vitiello, senior manager of field support for Medco Data in Fair Lawn, N.J., a unit of Merck & Co. Says Vitiello, "I toyed with it, did tests, but found it wasn't ready. I don't think my organization or many organizations have the manpower or the expertise to be jumping on this bandwagon right now. For asynchronous transfer mode, the problems are not quite yet."

By Joy Billups in New York

ED BY OTIS PORT

## P6: GANGING UP ON MAINFRAMES

YEARS, PUNDITS HAVE proclaimed that personal computer technology would bring an end to the need for mainframes. That may finally be approaching. On Oct. 16, Sequent Computer Systems Inc. in Marlborough, Ore., was to unveil a new family of machines that will bring together more than 100 Pentium Pro chips on one circuit board. Sequent will stuff as many as 60-odd such boards into its boxes. But the real key to harnessing this multiprocessor power is iQ-Link. This breakthrough technology makes it seem

Pentium Pro chips (previously called P6).

The new computers will build on Intel's plan to bundle up to four Pentium Pro chips on one circuit board. Sequent will stuff as many as 60-odd such boards into its boxes. But the real key to harnessing this multiprocessor power is iQ-Link. This breakthrough technology makes it seem

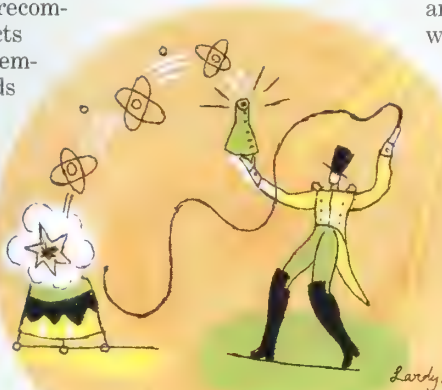
that all the digital data scattered around on the various boards are in one place. As a result, each chip can quickly access any information from this melded memory, and the computer can run existing software. It's similar to using many little TV sets to create one big composite display.

Pundits will still have to wait a bit before they can crow, though. Sequent's machine won't ship until late next year.

## LASER CHEMISTRY STARTS TO HEAT UP

SCHOOL, CHEMISTRY MAY appear to be an exact science. But industrial processes for making drugs, polymers, and other materials don't always work with textbook precision. One reason: Heat, the usual source of energy to break molecular bonds so atoms can recombine in new ways, acts unpredictably. So, if a chemist brews compounds that break down in more than one way, it will be hard to predict what's why. Scientists are now working to harness laser power. Researchers promise a way to deliver a precise amount of energy to break specific bonds—in short, a much better way to trigger chemical reactions. In the Oct. 6 issue of *Science*

magazine, one of the leading laser-chemistry teams reports making some major progress toward this goal. Robert J. Gordon, a chemistry professor at the University of Illinois at Chicago, says that a pair of lasers



have been used to "steer" a chemical reaction away from undesired outcomes, thus yielding far more of the desired product.

Two lasers with different wavelengths were fired at hydrogen disulfide molecules. By regulating their so-called phase difference—the locations of the crests and valleys of the light waves in the two beams—

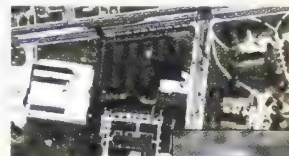
researchers were able to control how the molecules break apart.

Gordon says that his group started with two-atom molecules and is now working with five-atom ones. But, he admits, "that's still a long way from drug molecules," which are far larger.

An industrial-scale process will take at least a couple of more years of research.

## A SHARPER EYE IN THE SKY

UTILITIES, TELEPHONE companies, and government agencies spend a combined \$3 billion a year to collect geographic data to plot power lines, choose cellular transmission sites, and generate maps. While aerial photography produces images with razor-sharp detail, collecting the data for a large project can take months. Satellites can cover a lot more ground—



**FUZZBUSTER:** Before and after Space Imaging

and do it in the blink of an eye. But the photographs they produce are blurry. All that is about to change, says Space Imaging in Thornton, Colo.

In late 1997, Space Imaging plans to launch a satellite that will snap pictures with one-meter resolution. That means this bird sees objects as small as one square meter, a tenth the size of what today's commercial satellites can manage. Lockheed Martin Corp. and Eastman Kodak Co. helped develop its improved optics and global-positioning accuracy. The satellite will record a 50-square-mile area in less than three seconds. That should lead to drastic cost reductions and a raft of new consumer applications, including multimedia travel brochures that let virtual tourists fly over a beach resort before booking reservations.

## BEING SURE THESE VIDEOS TELL THE TRUTH

IT AIN'T NECESSARILY true anymore. Technology enables images to be edited and doctored to show—or not show—just anything. So when the International Atomic Energy Agency wanted to switch from film to digital video

cameras to check compliance with the Nuclear Nonproliferation Treaty, it had a problem: How could it be sure that the images hadn't been tampered with?

Cryptographic technology from RSA Data Security Inc. provides the answer. When the sealed video cameras that monitor nuclear-plant reactors and fuel-rod storage sites snap a picture, a computer chip attaches an encrypted

digital "signature." If the image is then altered in any way—before or during transmission to an orbiting satellite—the bogus data will be flagged when the signature is decrypted.

The filmless surveillance stations from Aquila Technologies Group Inc. in Albuquerque cost about \$25,000. Aquila says the system could readily be adapted for industrial security.



EDITED BY AMY DUNKIN

## TEST-DRIVING MANAGED CARE FOR YOUR CAR

**S**o you've had an auto accident. While the car sits idle in the shop, you're caught in the middle as the insurance company and the repair shop bicker over price. Sound familiar? The direct repair program (DRP), a little-known service offered by most of the major auto insurers, and the preferred provider option (PPO), which is available from only a handful of carriers, may help take the hassle out of the claims process. Think of it as managed care for car repair.

Similar to managed health-care plans, a DRP allows you to choose between prescreened network repair shops or your own mechanic. Using a participating DRP shop ensures that the insurance company covers all costs, except the deductible, and often guarantees the repairs as well. Without a DRP, policyholders must shop around for the best estimate—and keep their fingers crossed that insurers will agree to pay.

**UNADVERTISED.** Not all DRPs provide the same benefits, but for policyholders willing to comparison-shop, DRPs can offer greater convenience, cost savings, and better quality repairs.

All five of the top auto insurance carriers in the U.S. (State Farm, Allstate, Farmers Insurance Group, Nationwide, and USAA), which represent 50% of all insured cars, offer DRPs on a regional basis. According to the National Association of Independent Insurers, over one-quarter of policyholders with access to DRPs

choose them. So far, insurers say complaints are few.

Based on the success of DRPs, a few companies are experimenting with a more restrictive form of managed care: the PPO. Under this

system, policyholders trade choice for premium relief. PPOs require that you agree at the time of purchase to use only network repair shops in exchange for a discount on your collision or comprehensive premium, or a lower deductible. Going out of network and getting reimbursed even partially may not be an option. Read the fine print when entering a PPO, since some insurers are more inflexible than others.

DRPs are rarely advertised by insurers, so ask up front if a company has one. If so, request a list of repair shops near both your home and office. These shops are part of a network of garages that

has negotiated agreements with the insurer on labor rates and repair practices.

Choosing the DRP eliminates the need to shop for estimates because the network's garage is immediately authorized by the insurer to start the repairs. Some DRPs may even spring for a loaner car. Without delays caused by price disputes or waiting for a claims adjuster, your car is usually ready sooner. Using a DRP typically shaves off five to seven days from the time you file the claim until the repaired car is returned, according to Jack Rozint, senior vice-president at CCC Information Services,

a Chicago-based company specializing in automation of car insurance claims. Frequently, these age and/or the insurer company guarantee the pairs for as long as you own the car.

**STEADIER RATES.** Not surprisingly, DRPs also benefit insurers, saving an estimated \$255 for an average claim. \$1,800 to \$2,000, Rozint says. The savings stem from shortening the rental-car period for loaners, dispatching with an adjuster, computerizing the claims process, and negotiating discounts on parts and labor.

If DRPs cut costs, you



### INSURANCE

many insurers pass on savings to the consumer in the form of reduced rates? Companies respond that savings resulting from programs merely help keep rates stable. Comprehensive and collision have held very steady number of years and shown the same ram- increases as liability through the manage- of car-repair costs," Thom McDaniel, an ex- vice-president at CNA Insurance Cos. in Chicago. number of companies also test-driven PPOs.



waives \$50 of the annual deductible if the policyholder agrees at the time of the claim to use designated repair shops. "This admittedly small offer is very welcome to most people, especially at what can be a stressful time," says Progressive's Florida division president, Bob McMillan, who is based in Tampa.

Although McMillan says Progressive would like to roll out PPOs in other areas, there may be obstacles to a consistent nationwide program because auto insurance is regulated differently by each state. At present, for example, two states have specific restrictions on direct repair programs. Massachusetts bans insurer repair networks entirely. The state has concluded that it's a conflict of interest to have the insurance company promoting repair shops. In New York, insurers are only allowed to offer DRPs at the time of sale or if the customer requests a referral when filing a claim. New Jersey's Insurance Dept. recently passed a regulation mandating that any auto insurance company interested in establishing a PPO must give policyholders a discounted premium, one that is yet to be determined. Several carriers say they're waiting to see how deep the mandated discount is before plunging into managed coverage.

**SECOND OPINION.** But there's a downside. Although Bill Lawrence, manager of Allstate's 25-year-old DRP, says the Big Five insurers typically use high-tech procedures such as video imaging to assure that repairs are done correctly, some companies may have less rigorous quality controls. He suggests that policyholders always request an invoice detailing all repairs made and their cost. If you have any doubt that repairs were done, get a second opinion by taking the invoice to an independent shop: Many will check the work free of charge or for around \$25.

Another potential problem: too few repair locations. Troy Voght, a 24-year-old engineer in Orlando, jumped at his insurer's offer to reduce by

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vice-president at Merchant's, says policyholders who opt to receive the discount enter into a binding contract that requires them to use the company's referred shop. "I can't talk about an individual claim," Ward says. "We write \$10 million in Florida and have a very low

## What to Ask about Insurer Repair Networks

### DISCOUNTS

Does the insurer offer a premium break or a lower deductible on collision coverage if you agree to use only the recommended shops?

### AVAILABILITY

How many participating shops can you choose from near your home or job? And how many states besides your own have repair shops in the network, if you have an accident while traveling?

### DEPENDABILITY

Do the shops provide a written warranty for any work done, and how long will the insurer stand behind it?

### STANDARDS

What are the criteria for shop participation? Is the shop required to meet certain standards of equipment, training, and facilities?

### QUALITY

How often does the insurer reinspect the shops to ensure quality repairs?

### REPUTATION

Is the shop you intend to use the subject of any complaints filed with your state insurance department or local Better Business Bureau?

### EXTRAS

Do network shops offer a free rental car, or do you need extra rental coverage?

20% his premium for physical-damage insurance if he agreed at the time of sale to use the insurer's repair network. Ten days after buying the policy, a flash flood damaged Voght's car. The insurer, Merchant's & Business Men's Mutual, of Harrisburg, Pa., then told Voght his car would be taken to its direct repair shop over 200 miles away in Hollywood, Fla. Voght decided to have the repairs done out-of-network and agreed to pay the difference, but Merchant's refused and ordered the car to Hollywood—where it still sits today, almost 10 weeks later.

Charles Ward, a senior

complaint ratio. This is just one disgruntled claimant."

Nonetheless, the industry trend is toward car-repair networks. "Managed care seems to work with medical coverage, and it's supposedly helping reduce costs, so I think it can work for car repairs in the future," says Bill Mayer, assistant vice-president for claims at Government Employees Insurance Co. in Washington, D.C. He predicts GEICO eventually will offer a PPO. But unless auto insurance buyers are willing to sacrifice choice for savings, full-fledged managed care could be a bitter pill to swallow. *Kerry Capell*



# FOR PROBLEM DRINKERS, A MODERATE PROPOSAL

Michael Andes had been a social drinker since high school, but when he and his wife separated three years ago, he began to indulge nearly every day. The Ann Arbor (Mich.) social worker, 53, was downing roughly 35 glasses of beer or wine a week when friends expressed concern. Finally, a year ago, he enrolled in DrinkWise, a controversial new program that teaches drinkers to reduce their alcohol consumption before it gets out of hand. Andes says he feels much better now that he has cut his drinking by more than half.

But the controlled drinking approach advocated by DrinkWise and Moderation Management (MM), a self-help group with chapters in eight cities, is considered heresy among those who adhere to 12-step programs such as Alcoholics Anonymous. In the U.S., abstinence has long been the only accepted treatment goal for heavy drinkers, unlike some European countries where moderation is widely accepted. "Since the 1960s, we've thought there are two kinds of people," says Dr. William R. Miller, professor of psychiatry at the University of New Mexico. "Either you're an alcoholic or you aren't."

**MISLABELED.** However, nearly 20 years of research suggests that drinkers encompass a broad spectrum and that many were mislabeled alcoholics. Studies show one-third of the U.S. adult population doesn't touch the stuff. Of the remaining two-thirds, 75% are considered social drinkers who imbibe occasionally. Some 20% are problem drinkers with some physical dependence on alcohol, which

may have led to job, relationship, health, or financial strains. The last 5% are severely dependent on alcohol and suffer withdrawal and other symptoms typically associated with alcoholism.

The problem drinkers are the ones moderation programs target. Of the 73 DrinkWise graduates, 72% hold professional or managerial jobs, and 52% report that prior to entering the program, their problem drinking had gone on for two years or less, suggesting their habit is not chronic. "People who find our program appealing don't think they're powerless over alcohol," says Keith Bruhnson, program manager for DrinkWise, which originated last year at the University of Michigan.

If you enroll in DrinkWise or become an MM member, abstinence is necessary only if moderation doesn't work. Both programs offer similar guidelines. Men are allowed a maximum of 12 drinks a week and women 9, with no more than 4 on any day for men and 3 for women. The guidelines are based on studies by Toronto's Addiction Research Foundation, which show that drinkers who stay within those limits experience few, if any, alcohol-related side effects.

DrinkWise (800-222-5145) offers one-on-one meetings with trained counselors or group sessions in Ann Arbor and Philadelphia. It plans to open offices

in Detroit in November. A nationwide program is also available via telephone. You must first submit to an interview with a counselor, who ascertains your suitability for the program and sets goals. After you abstain for two weeks, you'll speak in person or by phone with a counselor for three 45-minute sessions over eight weeks. The counselor will teach you strategies for curbing your drinking, such as keeping a diary of temptations and how you coped with them. The program costs \$595 in person and \$395 by phone and includes two follow-up sessions at three and nine months.

MM will soon start support groups in 40 more cities. If you join, you must abstain for one month. Then, MM recom-

mends nine steps to achieve moderation: "make positive lifestyle changes." You'll discuss what you've learned and how you're doing at weekly, one-hour meetings. Most members don't attend every week; the first couple of months there's no cost, although it accepts donations. Many participants buy founder Al Kishline's 1994 book *Moderate Drinking: The Moderation Management Guide for People Who Want to Reduce Their Drinking* (Crown). An updated version of the book will be published in January. For a list of groups in your area, send a self-addressed stamped envelope to MM, P.O. Box 6005, Ann Arbor, Mich., 48106.

**HARMFUL?** Although participants in moderation programs have cut back on drinking, some experts have reservations. "Moderation might be potentially harmful for alcoholics who love to be alcoholics," says Dr. Richard Fuller, director of the division of Alcohol and Prevention research at the National Institute on Alcohol Abuse and Alcoholism. AA declines comment, citing the first of its Twelve Traditions: "We have no opinion on outside issues."



## Steps to Controlled Drinking

- Abstain from alcohol for two to four weeks.
- Scrutinize your drinking habits—how often, how much, where, and with whom. Keep a drinking diary.
- Examine what triggers you to drink.
- Take no more than 12 drinks per week if you're a man, 9 if you're a woman.
- Drink no more than 4 alcoholic beverages on any given day if you're a man and 3 if you're a woman.
- Imbibe a maximum of three days a week.
- Don't drink more than 1 drink per hour.

DATA: DRINKWISE, MODERATION MANAGEMENT

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***e Means to Make Better Decisions***

Providing the means to deliver accurate and timely information to improve work processes and make better business decisions is the job of George Alameda, Chevron U.S.A. Production Company's Manager of Information Technology.

The company is using the SAS System to help with enterprise-wide information delivery. "Our mission is to make financial, operational, and reservoir data available in easy-to-use format to all the asset teams at work in SA Production Co.," says Alameda. "We've found the SAS System is a superior solution for analyzing data, turning data into useful metrics, and guiding our cross-functional teams toward improved work processes."

One team, in CUSA Production's Western Business Unit, is tracking the profitability of individual wells. "It's tremendously difficult task to optimize our field operations for maximum profitability," says Alameda.

"With the SAS System, we can integrate large amounts of data and build a picture to compare one field against another and challenge our asset teams to identify and share best operating practices."

***Reaching for the Best***

Alameda looks forward to extending the use of the metrics and performance monitoring data to employees trying to improve their work processes. He admits

his vision is far reaching, but so is the SAS System. "Our challenge is to be better than the best," he concludes, "and the SAS System is helping us reach that goal."

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*The SAS System*

***Executive Summary***

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## PRICIER HOTELS ARE PILING ON THE EXTRAS

Gone are the days of the early 1990s, when you could haggle at the front desk of a hotel and get a \$150 room for just \$100. Rising occupancies because of a loosening of business travel dollars, an increase in domestic tourism, the lack of new hotel construction, and a reduction in operating expenses have made hotels more profitable and less desperate to put heads in beds.

But while most major lodging chains have dumped the discounts and jacked up room rates 3% to 5% annually in the past two years, they're loath to lose your personal or corporate business to less expensive competitors. So hoteliers are scrambling to offer more for your money in the form of value-added promotions. "It's very clear that hotel chains are upgrading their services to justify their rates," says Douglas Shifflet, president of D.K. Shifflet & Associates, a McLean (Va.) travel research firm.

Programs aimed at leisure travelers hope to tempt you with extras such as complimentary breakfast and free

stays for the kids. For example, Radisson's Bed & Breakfast Breakaways package offers a full breakfast for two (worth \$12 per person) at the room rate, which averages \$84.40 per night. That's only \$5 more than the same room without breakfast included. Similarly, Holiday Inn Worldwide's Best Breaks features a room and breakfast for two at a rate that is less than if breakfast were added on to the bill, says Craig Hunt, vice-president for worldwide franchising.

By tacking on some restrictions, other companies are able to bundle in more extensive services. ITT Sheraton, for one, offers some meals, accommodations for children at no charge, and room upgrades at full rates under its Family and Romance Vacation packages. The

catch is that you have to stay for a minimum of two or three nights.

The programs are available at 19 hotels, mostly in California, Florida, and Hawaii and will be beefed up in 1996, says David Kalsbeek, senior vice-president and director of marketing and strategic planning.

**MOBILE DESKS.** Not surprisingly, some of the best deals

are reserved for business travelers who usually pay premium rates. But check ahead when booking. These services, which may include in-room fax machines, special desks, and current-release movies, are not offered at every property in every chain, and some hotels throw in more than others. "Some of our travelers find these rooms worth the money, especially if they need to use certain business services every day," says Peter Buch-

heit, director of travel meeting services at Black Decker in Towson, Md.

Each of Radisson's Business Class rooms in 201 hotels provides newspaper, movies, coffee, breakfast, local phone service, fax, receipt and delivery, and computer hookup. These rooms average \$20 per night above the corporate rate for suites worth \$35 to \$50, says Geoff Rochester, senior vice-president for marketing at Radisson Hotels Worldwide.

Clarion charges a \$20 premium above the average rate for the Business Room, as does Westin's Guest Office. The latter, in addition to offering special phones and some free amenities, includes the use of a fax machine, and copies of health-club access. Westin is rolling out the program at 32 hotels initially. Major International's upscale service hotels offer a Room That Works at no extra charge. Currently, at properties, it will be a

## Hotel Value Deals

Here are some hotels that offer extras, usually at a premium charge.

| COMPANY                           | PROGRAMS*                                                                                                                              |
|-----------------------------------|----------------------------------------------------------------------------------------------------------------------------------------|
| <b>CLARION</b><br>800 CLARION     | Special business room. Rate premium, \$20. Value, \$40.                                                                                |
| <b>HOLIDAY INN</b><br>800 HOLIDAY | Breakfast package. Value per room per night, \$12.                                                                                     |
| <b>HYATT</b><br>800 233-1234      | Special business room. Rate premium, \$15. Worth \$40 to \$95.                                                                         |
| <b>MARRIOTT</b><br>800 228-9290   | Special business room, no extra cost. Average room rate is \$99.50.                                                                    |
| <b>RADISSON</b><br>800 333-3333   | Bed-and-breakfast program. Value, \$24 per room (for two). For business travelers, special room for \$20 premium. Value, \$35 to \$50. |
| <b>SHERATON</b><br>800 325-3535   | Family and Romance packages, offering extras, at full rate.                                                                            |
| <b>WESTIN</b><br>800 228-3000     | Special business room. Rate premium, \$20. Worth \$75 to \$200.                                                                        |

\* Business rooms include special services, in-room office equipment, or extra amenities.

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†† See limited warranty & restrictions at dealer. Excludes normal maintenance & wear items.



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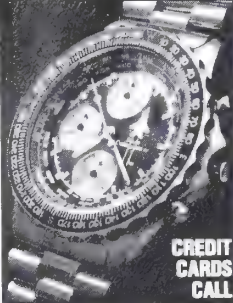
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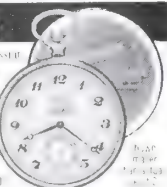


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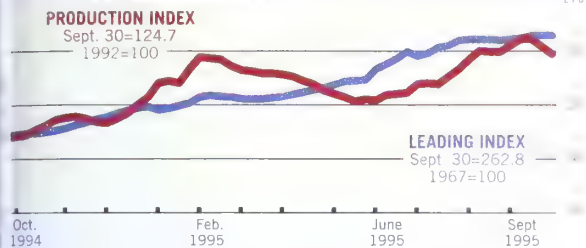
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## DUCTION AND LEADING INDEXES

Change from last week: -0.6%  
Change from last year: 7.4%



These are 4-week moving averages.  
The production index fell during the week ended Sept. 30. Before calculation of the four-week moving average, the index rebounded to 124.5, from 123.3, as in the seasonally adjusted output of trucks and rail-freight traffic led the index. For September, the index fell to 124.7 from 125.4 in August.  
The leading index was unchanged in the latest week. The unaveraged index rose to 262.4 from 262.6. For the month of September, the index rose to 262.1 from August's reading of 262.1.

Sources: U.S. Commerce Dept. (production index); The McGraw-Hill Companies (leading index); Bureau of Economic Analysis (unaveraged index).

## FINANCIAL INDICATORS

|                                            | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|--------------------------------------------|-------------|------------|--------------|
| <b>STOCK PRICES</b> (10/7) S&P 500         | 582.13      | 582.91     | 27.4         |
| <b>LIBOR RATE BOND YIELD, Aaa</b> (10/7)   | 7.20%       | 7.33%      | -16.0        |
| <b>COMMODITY MATERIALS PRICES</b> (10/7)   | 111.6       | 112.2      | NA*          |
| <b>TELEPHONE SERVICE FAILURES</b> (9/29)   | NA          | 313        | NA           |
| <b>REAL ESTATE LOANS</b> (9/27) billions   | \$497.3     | \$496.3r   | 11.9         |
| <b>MORTGAGE SUPPLY, M2</b> (9/25) billions | \$3,723.2   | \$3,722.8r | 4.0          |
| <b>UNEMPLOYMENT CLAIMS</b> (9/23) thous    | 335         | 366        | 8.1          |

Sources: Center for International Business Cycle Research (CIBCIR), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures companies), Federal Reserve, Labor Dept. CIBCIR seasonally adjusts data on failures and real estate loans. \*Historical data available from CIBCIR.

## INTEREST RATES

|                                               | LATEST WEEK | WEEK AGO | YEAR AGO |
|-----------------------------------------------|-------------|----------|----------|
| <b>MUTUAL FUNDS</b> (10/10)                   | 5.74%       | 5.75%    | 4.62%    |
| <b>COMMERCIAL PAPER</b> (10/10) 3-month       | 5.83        | 5.81     | 5.51     |
| <b>LIBOR RATES OF DEPOSIT</b> (10/11) 3-month | 5.79        | 5.78     | 5.49     |
| <b>MORTGAGE</b> (10/6) 30-year                | 7.78        | 7.89     | 9.03     |
| <b>FIXED RATE MORTGAGE</b> (10/6) one-year    | 5.82        | 5.79     | 5.80     |
| (10/11)                                       | 8.75        | 8.75     | 7.75     |

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### STOCK INVENTORIES

Oct. 16, 10 a.m. ▶ Inventories of manufacturers, wholesalers, and retailers probably rose a small 0.2% in August, according to the median forecast of analysts surveyed by MMS International, The McGraw-Hill Companies. Inventories rose 0.3% in July. Business sales increased a healthy 1.5%, after falling 0.3% in July. That's indicated by the sales already reported by manufacturers and retailers.

### INDUSTRIAL PRODUCTION

Oct. 17, 9:15 a.m. ▶ The MMS estimate is that output at U.S. factories, and utilities was probably

unchanged in September from August's level. That's suggested by the flat reading of total hours worked in the manufacturing sector last month. Output jumped 1.2% in August, helped by increased auto and truck production. Operating rates for all industry likely stood at 84% last month, down from 84.3% in August.

### INTERNATIONAL TRADE

Wednesday, Oct. 18, 8:30 a.m. ▶ The foreign trade deficit for goods and services probably narrowed slightly, to \$11 billion in August, projects the median MMS forecast. The July trade gap stood at a large \$11.5 billion. Exports, which have fallen for two consecutive months, likely rebounded.

Imports, also down for two months in a row, probably were a bit higher in August as well. Foreign trade continues to be a severe barrier to U.S. economic growth.

### HOUSING STARTS

Thursday, Oct. 19, 8:30 a.m. ▶ The MMS survey projects that housing starts were little changed in September, from August's annual rate of 1.4 million. Starts in August were only slightly ahead of July's pace. But single-family homebuilding showed more strength, rising by 1.4% in August. As consumers begin to worry again about job prospects, mortgage applications to buy a home have flattened out. That means home buying and construction should weaken this winter.

## PRODUCTION INDICATORS

|                                                        | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|--------------------------------------------------------|-------------|-----------|--------------|
| <b>STEEL</b> (10/7) thous. of net tons                 | 1,951       | 1,934#    | 1.2          |
| <b>AUTOS</b> (10/7) units                              | 135,355     | 141,900r# | 0.8          |
| <b>TRUCKS</b> (10/7) units                             | 127,141     | 127,757r# | 9.4          |
| <b>ELECTRIC POWER</b> (10/7) millions of kilowatt-hrs. | 59,654      | 58,979#   | 4.2          |
| <b>CRUDE-OIL REFINING</b> (10/7) thous. of bbl./day    | 14,217      | 14,489r#  | 3.3          |
| <b>COAL</b> (9/30) thous. of net tons                  | 20,641#     | 20,650    | -0.4         |
| <b>PAPERBOARD</b> (9/30) thous. of tons                | 855.8#      | 860.5r    | -6.5         |
| <b>PAPER</b> (9/30) thous. of tons                     | 821.0#      | 832.0r    | -1.3         |
| <b>LUMBER</b> (9/30) millions of ft.                   | 481.2#      | 477.7     | 0.0          |
| <b>RAIL FREIGHT</b> (9/30) billions of ton-miles       | 25.6#       | 25.3      | 2.4          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WPA, SFPA, Association of American Railroads

## PRICES

|                                                             | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|-------------------------------------------------------------|-------------|----------|--------------|
| <b>GOLD</b> (10/11) \$/troy oz.                             | 384.500     | 382.500  | -1.4         |
| <b>STEEL SCRAP</b> (10/10) #1 heavy, \$/ton                 | 140.50      | 143.50   | 5.2          |
| <b>COPPER</b> (10/6) \$/lb.                                 | 133.8       | 136.7    | 10.1         |
| <b>ALUMINUM</b> (10/6) \$/lb.                               | 81.5        | 82.0     | 1.9          |
| <b>COTTON</b> (10/6) strict low middling 1-1/16 in., \$/lb. | 88.41       | 88.65    | 33.4         |
| <b>OIL</b> (10/10) \$/bbl.                                  | 17.28       | 17.57    | -2.4         |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

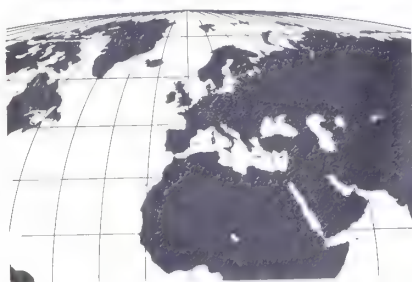
## FOREIGN EXCHANGE

|                                | LATEST WEEK | WEEK AGO | YEAR AGO |
|--------------------------------|-------------|----------|----------|
| <b>JAPANESE YEN</b> (10/11)    | 101.01      | 101.17   | 99.94    |
| <b>GERMAN MARK</b> (10/11)     | 1.42        | 1.44     | 1.54     |
| <b>BRITISH POUND</b> (10/11)   | 1.57        | 1.58     | 1.59     |
| <b>FRENCH FRANC</b> (10/11)    | 4.98        | 4.96     | 5.27     |
| <b>ITALIAN LIRA</b> (10/11)    | 1606.5      | 1613.3   | 1570.4   |
| <b>CANADIAN DOLLAR</b> (10/11) | 1.33        | 1.33     | 1.35     |
| <b>MEXICAN PESO</b> (10/11)    | 6.745       | 6.535    | 3.417    |

Sources: Money, Bank, Finance, Current Exchange Rates, Oct. 1995, except for British pound in dollars



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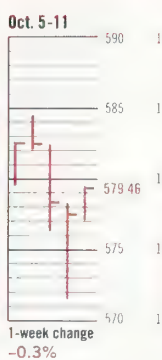
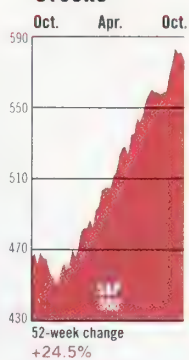
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# Investment Figures of the Week

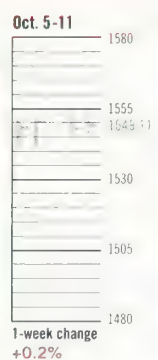
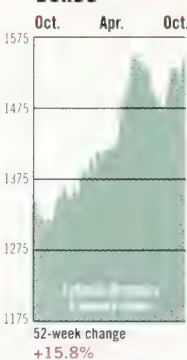
## STOCKS

Stocks went on a roller-coaster ride after Inc.'s announcement that it met fourth-quarter earnings estimates helped spark a sell-off in the NASDAQ Composite Index on Oct. 9. The NASDAQ and the High Tech Index regained ground later in the week as bonds edged, with the yield on the Treasury staying at 6.43%. Mutual funds, the Warburg Investor Japan OTC Fund, with brightenings in tech and retail became the four-week leader return.

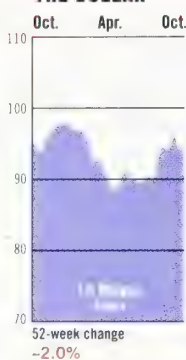
## STOCKS



## BONDS



## THE DOLLAR



## MARKET ANALYSIS

|                              | Latest | % change |         |
|------------------------------|--------|----------|---------|
|                              |        | Week     | 52-week |
| INDUSTRIALS                  | 4735.3 | -0.1     | 22.2    |
| COMPANIES (S&P MidCap Index) | 209.9  | 0.1      | 20.0    |
| COMPANIES (Russell 2000)     | 297.9  | -1.0     | 16.9    |
| COMPANIES (Russell 3000)     | 331.9  | -0.3     | 24.0    |

|                      | Latest   | % change (local currency) |         |
|----------------------|----------|---------------------------|---------|
|                      |          | Week                      | 52-week |
| FINANCIAL TIMES 100) | 3474.3   | -2.0                      | 12.1    |
| NIKKEI INDEX)        | 17,891.2 | -1.4                      | -10.9   |
| (TSE COMPOSITE)      | 4474.6   | -0.4                      | 2.7     |

## FUNDAMENTALS

|                              | Latest | Week ago | Year ago |
|------------------------------|--------|----------|----------|
| 90-DAY TREASURY BILL YIELD   | 5.45%  | 5.45%    | 5.12%    |
| 30-YEAR TREASURY BOND YIELD  | 6.43%  | 6.43%    | 7.89%    |
| S&P 500 DIVIDEND YIELD       | 2.35%  | 2.34%    | 2.75%    |
| S&P 500 PRICE/EARNINGS RATIO | 16.7   | 16.8     | 18.3     |

## TECHNICAL INDICATORS

|                                           | Latest | Week ago | Reading  |
|-------------------------------------------|--------|----------|----------|
| S&P 500 200-day moving average            | 524.6  | 521.6    | Positive |
| Stocks above 200-day moving average       | 67.0%  | 71.0%    | Neutral  |
| Speculative sentiment: Put/call ratio     | 0.76   | 0.66     | Positive |
| Insider sentiment: Vickers sell/buy ratio | 2.63   | 2.72     | Negative |

BLOOMBERG FINANCIAL MARKETS

## INDUSTRY GROUPS

### MONTH LEADERS

|                             | % change |          |
|-----------------------------|----------|----------|
|                             | 1-month  | 12-month |
| DRUGS                       | 13.6     | 58.2     |
| BEVERAGES                   | 12.6     | 49.7     |
| TELECOM                     | 12.2     | 35.6     |
| TELECOM                     | 12.0     | 32.9     |
| DISTANCE TELECOMMUNICATIONS | 11.4     | 14.1     |

### Strongest stock in group

|               | % change |          | Price   |
|---------------|----------|----------|---------|
|               | 1-month  | 12-month |         |
| Pfizer        | 17.0     | 54.7     | 55      |
| Pepsico       | 13.4     | 59.6     | 51 1/8  |
| Philip Morris | 14.0     | 41.3     | 84 3/4  |
| Nike          | 19.9     | 80.1     | 109 1/8 |
| AT&T          | 14.6     | 19.7     | 63      |

### MONTH LAGGARDS

|                          | % change |          |
|--------------------------|----------|----------|
|                          | 1-month  | 12-month |
| AND GLASS CONTAINERS     | -18.6    | -1.6     |
| COMMUNICATIONS EQUIPMENT | -16.2    | 39.5     |
| TELECOM                  | -15.4    | -28.7    |
| CONDUCTORS               | -13.9    | 75.5     |
| SPECIALIZED MACHINERY    | -13.9    | 6.4      |

### Weakest stock in group

|                         | % change |          | Price  |
|-------------------------|----------|----------|--------|
|                         | 1-month  | 12-month |        |
| Crown Cork & Seal       | -19.7    | -3.0     | 36 1/8 |
| Scientific Atlanta      | -36.0    | -36.0    | 13 1/8 |
| Inland Steel Industries | -24.7    | -42.6    | 21 3/4 |
| Micron Technology       | -25.3    | 282.2    | 67 1/8 |
| Caterpillar             | -24.1    | -1.4     | 52 1/8 |

## MUTUAL FUNDS

MORNINGSTAR INC.

### 5

| 5-year total return          | %   |
|------------------------------|-----|
| JRG PINGUS ADVISOR JAPAN OTC | 7.8 |
| IN HILL MUTUAL               | 6.9 |
| US EDISON ELECTRIC INDEX     | 6.7 |

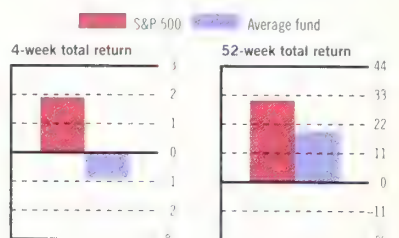
| total return          | %    |
|-----------------------|------|
| TY SELECT ELECTRONICS | 94.1 |
| CAPITAL APPRECIATION  | 80.5 |
| TY SELECT COMPUTERS   | 77.6 |

### LAGGARDS

| Four-week total return                | %     |
|---------------------------------------|-------|
| MITCHELL HUTCH/KIDDER EQUITY-INCOME A | -13.2 |
| RESERVE INFORMED INVESTORS GROWTH     | -13.1 |
| WRIGHT EQUIFUND-MEXICO                | -12.8 |

| 52-week total return                | %     |
|-------------------------------------|-------|
| WRIGHT EQUIFUND-MEXICO              | -52.0 |
| BT INVESTMENT LATIN AMERICAN EQUITY | -38.1 |
| TCW/DW LATIN AMERICAN GROWTH        | -37.0 |



## RELATIVE PORTFOLIOS

DR/MCGRAW HILL

Portfolios represent the value of \$10,000 one year ago

Percentages indicate total returns

Treasury bonds  
**\$12,860**  
+0.65%

U.S. stocks  
**\$12,746**  
-0.83%

Foreign stocks  
**\$10,915**  
-0.48%

Money market fund  
**\$10,548**  
+0.12%

Gold  
**\$9,753**  
+0.76%

Figures on this page are as of market close Wednesday, Oct. 11, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are

as of market close Oct. 10. Mutual fund returns are as of Oct. 6. Relative portfolios are valued as of Oct. 10. A more detailed explanation of this page is available on request. r=revised



## A MINISTRY OF BLUNDERERS

Japan's elite Ministry of Finance is losing its standing within the global banking community. For the past five years, it has participated in a coverup of Japan's immense banking crisis, withholding vital information on up to \$1 trillion in problem loans—from not only the Japanese public but also central bankers around the world, including the U.S. Federal Reserve.

Now it appears that the MOF may have skirted American law by not notifying the Fed for at least six weeks this summer about a \$1.1 billion bond trading loss in the New York branch of Daiwa Bank Ltd. At the least, it is an egregious breach of trust among international bank regulators facing global financial meltdowns, such as Mexico's last year.

At worst, the delay could be part of a long-term pattern of MOF bureaucrats withholding information. We know that on Aug. 8, Akira Fujita, president of Daiwa, told Yoshimasa Nishimura, MOF Banking Bureau director general, about the \$1.1 billion in losses incurred in New York over 11 years. But the MOF sat on that information until Sept. 18.

Paradoxically, the MOF's disregard of the Fed came during the same summer months that the Fed and the U.S. Treasury were secretly organizing a plan to rescue Japan's financial system. Alarmed by what they saw as a looming Japanese banking crisis, U.S. officials boosted the dollar 26% against the yen, sending billions into Japanese corporate coffers. That pushed stocks up, increasing the capital of Japanese banks. Through the entire exercise, the Fed could not get correct figures on Japanese problem loans from the MOF.

The cost of the MOF's blunders has been high—no growth in Japan for years, a huge trade surplus, a wildly exaggerated yen, and a hollowing out of the economy. A high price indeed.

## LEAVE THOSE PENSION FUNDS ALONE

Who "owns" the \$100 billion in surplus money in Corporate America's pension plans, the retirees or the companies? Either way, Congress' proposal to allow corporations to tap surplus pension funds is a bad idea. It's a short-term policy that will generate quick tax bucks to help balance the budget at the expense of overall savings in the nation. It may be good for companies, it may not even hurt retirees, but it is bad government policy.

Virtually all U.S. retirement plans are shaped by the government's need for revenue rather than the family's or the economy's need for savings. Employee contributions to 401(k) plans are capped by the government at \$9,240. This year, Congress actually cut the 401(k) contribution by not compen-

sating for inflation. It needed more tax income to make a cut in revenues that occurred when trade tariffs were reduced. That's ridiculous, given that if people with 401(k)s could sock away more money for retirement, more would be available for economic growth and jobs.

The limits on individual retirement accounts are getting tighter—\$2,000 if you are not in another pension plan. Self-employed people with Keoghs get a much better deal: They can save up to \$30,000 or 15% of their income annually, tax-free. If entrepreneurs can save that much for the future, why not corporate employees? Washington should be encouraging all to put more money into pension plans, not

## BAUSCH & LOMB'S DISTORTED VISION

Tie the chief executive's compensation to company earnings, produce goods in high demand around the world, decentralize operations, and give the heads of business units tough quarterly growth targets to meet. That's the prescription for success in the tough new global economy, right?

Well, not always. BUSINESS WEEK's Cover Story on Bausch & Lomb Inc. illustrates how even the best business strategy can have unintended consequences when the corporate culture goes sour. A tenacious drive to meet the numbers comes with lax controls can derail even the best of companies.

For many years, shareholders certainly counted Bausch & Lomb as one of the very best. When Daniel E. Gill came to Bausch & Lomb in 1978, the maker of soft contact lenses, binoculars, and eyeglasses had revenues of \$442 million. By 1993, under his numbers-oriented, demanding leadership, B&L had sales of \$1.87 billion and earnings from continuing operations of \$193 million.

But something was rotten inside B&L. During Gill's reign, the heads of operations pumped sales to a degree unseen in most other companies. Double-digit increases were demanded every quarter, every year, regardless of local economic conditions. That led, in many operations, to phony invoices, sending goods to gray markets in Asia and the Middle East, and questionable accounting for sales.

It all worked until mid-1994. B&L discovered it had an enormous unsold inventory in Hong Kong. The head of Hong Kong operations took early retirement. In November, contact lens wearers brought a class action alleging that B&L had charged them different prices for the same lenses. In December, the Securities & Exchange Commission launched an investigation into whether or not B&L's contact lens division improperly inflated sales and profits in 1993. All in all, continuing earnings plunged 54% to \$88.5 million in 1994, as sales fell.

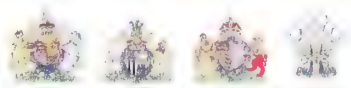
Gill says that B&L's problems are due to overambitious and incompetent divisional executives. Interviews with a cross-section of current and former B&L executives around the world suggest a different truth: It's up to the CEO of any company to make sure that good results aren't achieved by unrealistic targets, accounting irregularities, and ethical lapses.



## School in Britain is rarely cancelled.

Sometimes going to class requires more than a will to learn. The Discovery requires permanent four-wheel drive, all-terrain ABS, and a 4.0-liter V8 engine. All of which have made the Land Rover Discovery quite popular for plowing through the iciest corners of the United Kingdom. It was also the first 4x4 to provide the touring comfort of dual airbags. And with the reinforced strength of

its 14-gauge steel chassis, side impact beams, and steel inner body cage, the Discovery is undoubtedly built to last. Perhaps even through graduate school.



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So why not call 1-800-FINE 4WD for the dealer nearest you?

We must warn you, though.

Even with available seating for seven, only one person can truly appreciate the Discovery.

The rest have to go to school.

Always use your seatbelts. SRS/airbags alone do not provide sufficient protection.



*Jane Edwards  
Branch Manager  
Kelly Services*



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# IBM

## GERSTNER'S GROWTH PLAN

Yes, the CEO does have a vision. It's called network-centric computing. Here's an inside look.

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Well, that takes several companies. Companies like Microsoft, with whom we created the ideal platform for Windows NT and BackOffice, integrating hardware, software, and server management. Novell, with whom we've created networking standards for years. Oracle, whose databases are far easier to deploy on a Compaq server thanks to our partnership. And SAP, a leader in client/server applications, who's named us Partner of the Year.

You see, they may be Compaq servers. But they are Compaq-Microsoft-Oracle-SAP-Intel-Novell-SCO-Sybase-Cheyenne solutions. (We just couldn't fit all those logos on them.)

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# BusinessWeek

OCTOBER 30, 1995

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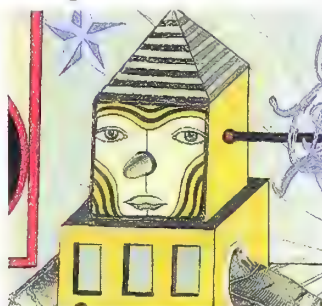


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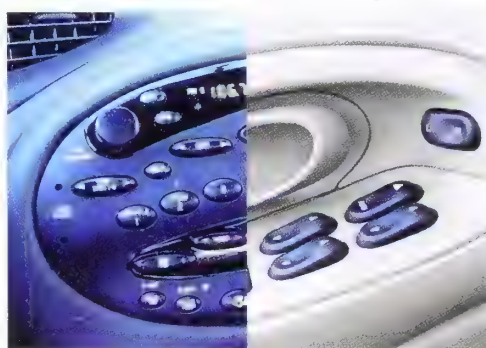


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# Up Front

EDITED BY LARRY LIGHT, WITH OLUWABUNMI SHABI

## UNREAL ESTATE

### ONE MORE CHORUS OF HEARTBREAK HOTEL

THE BAD NEWS isn't over for hotels. Sure, occupancy and rental rates are way up from the industry's 1990-91 doldrums. And hotel chains' profits are surging. Still, the chains typically just franchise their names and reservations services. It's the partnerships, usually local investors, that own the hotels and are in for a spate of foreclosures and bankruptcies.



LA CONCHA: Inn debt

Why? Some heavy loans are coming due that investors can't repay—or refinance. The sad tale started in the booming 1980s, when hotels borrowed huge sums, often with little down. Then the recession hit. Even though many hotels' valuations drooped, many lenders reluctantly restructured the loans, but only for scant two- to four-year terms. Well, time's

**TALK SHOW** “Everybody makes mistakes. My view is be- you accept money doesn't mean you agree with their agen-

—Senator Bob Dole, saying his Presidential campaign was wrong to return a \$1,000 donation from a gay GOP group



## CAPITAL OFFENSES

### CIRCLE THE PHONE SERGEANT

THE DEFENSE DEPT., of the \$700 toilet seat, target of wastebusters. This time, the Pentagon phones are in the crosshairs.

Every federal agency now required to use Sam's new Federal Tele System 2000, an AT&T collaboration that offers even better than the consumer long-distance. But the Pentagon—the government's biggest phone bill with 50% of the \$2.8 billion annual phone bill—has resisted using FTS. The military argues that FTS can't meet its security needs. So it buys phone service separately, usually straight from AT&T.

Result: The Pentagon pays \$300 million a year too much, says Congress' General Accounting Office. Now, Sprint—wants a piece of military's phone bill via FTS—has been outbidding Capitol Hill. Speaker of the House Majority Leader Bob Dole (Kan.) has told Defense Secretary William Perry that the Pentagon is “wasting billions of dollars.” Emmett Paige, assistant defense secretary, suggests that Dole is kidding to Westwood (Kan.) is Sprint because it is headquartered in his home state. A Dole aide denies that regardless, the Pentagon has begun shifting a small amount of its phone traffic to cheaper FTS. Mark Ly

## AFTER NAFTA

### HEY, IT'S NOT REALLY 'WINE' EITHER



NORTHERN LITES: Uncool?

ARE THINGS really wastin' away in Margaritaville? Mexican government officials think so. They are complaining to U.S. trade officials that Seagram and E&J Gallo Winery are selling margarita-flavored coolers that lack a critical ingredient: tequila.

Under the North American Free Trade Agreement, only Mexico can produce tequila—made from the blue agave plant. And Mexico is worried that cheaper wine- or malt-based margarita coolers will water down its \$1.2 billion U.S. market. Introduced over the past two years, the Seagram and Gallo products are “unfair competition,” fumes German Cava- zos, deputy director of Mexico's Office of Standards.

Heublein, which sells Jose Cuervo tequila, also has entered the fray, filing a petition with Washington and lawsuits. The suits seek unspecified damages and a court order barring Heublein's rivals from calling anything a margarita unless it contains tequila.

U.S. trade officials are taking Mexico's complaint with a shaker of salt. So are Gallo

and Seagram, which say their products are clearly and accurately labeled. Plus, Seagram accuses Heublein of hypocrisy, since in 1993 Heublein test-marketed a “Moscow Margarita” that used vodka instead of tequila. Heublein, which pulled the product, says its label made obvious what was and wasn't inside.

Stan Crock

## THE LIST AIR FARE

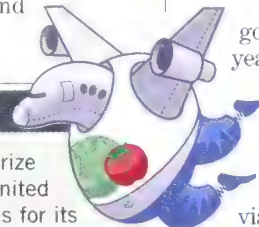
In-flight meals may not taste good, but at least you can order a health platter that's good for you, right? Uh, maybe not. A doctors' group asked airlines for a sample of their vegetarian dishes. The worst had 31% to 39% fat, not as good as skinless baked chicken (around 25%)—and almost as bad as beef (40% to 50%). Lowest-ranked Northwest's Bombay curry is fried in fatty vegetable oil, the docs say. Northwest insists it has less-fatty dishes and denies it submitted any dishes for the test.

For those who prize their arteries, United Airlines triumphs for its soy-based vegetarian steak.

### AIRLINE HEALTH-PLATTER RANKING

|             | Representative vegetarian meal | Fat content |
|-------------|--------------------------------|-------------|
| UNITED      | Vegetarian steak               | 3%          |
| TWA         | Stuffed peppers                | 8           |
| CONTINENTAL | Bean chili w/ nuts             | 28          |
| USAIR       | Baked barley                   | 31          |
| AMERICAN    | Vegetarian pasta               | 33          |
| NORTHWEST   | Bombay curry                   | 39          |

NOTE: Delta did not participate  
DATA: PHYSICIANS COMMITTEE FOR RESPONSIBLE MEDICINE





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## SMUGGLER'S PARADISE

### ONE BIG DUTY-FREE SHOP

THE RUSSIAN DISTRIBUTOR OF Mexico-brewed Corona beer figures that, given an import tax of \$1.40, rival beers should cost at least \$2.50 a bottle. Try \$1. How come?

Sharp variations in retail prices of imported goods—

## RUSSIA: Customs check

from beer to luxury cars—reflect the sorry state of Russia's customs authorities. They are budgeted to collect \$2 billion in taxes and duties this year. But because of corruption, smuggling, and poor organization, they'll be lucky to get a third of that. Undercut by rivals with sweet customs deals, honest importers must shave margins to stay competitive. In Moscow, the minimum price for a pack of top-quality cigarettes should be more than \$1. Yet it's often as low as 50¢, since shady importers bribe officials.

Pressured by the International Monetary Fund to up its revenues, Moscow is getting tougher on the most obvious scams. Imported cigarettes and booze now must carry a government tax stamp or face confiscation. Critics, though, doubt corrupt officials will really thwart smugglers. *Geoff Winestock*

## AFTERLIVES

### CAN HE BOUNCE BACK WITH BIOTECH?

HIS NAME ONCE was up there with Digital Equipment's Kenneth Olson and Wang Laboratories' An Wang as one of the leading lights of the computer industry. Then Edson de Castro, co-founder of Data General in 1968, saw his company go into decline: It didn't make the shift from mini-computers to personal computers. In 1990, the board ousted him.

Now, de Castro, 57, is plunging into a business he thinks holds as much promise as computer making. He's chairman of Xenometrix, a small Boulder (Colo.) biotech company that makes kits for drug and cosmetics outfits to



DE CASTRO: Testing

test products in vitro for possible side effects—thus reducing the need for test animals. Biotech "feels like the computer industry a generation ago," says de Castro, who joined Xenometrix in 1992. He has filed to take it public.

Unfortunately, biotech is a crowded field fraught with disappointment. Technical hurdles have stymied other companies that tried to replace animal testing. With only \$514,000 in revenue for the year ending June 30, Xenometrix has yet to turn a profit. Still, it has attracted high-profile Mary Kay cosmetics, which is working with it on a skin irritation test. *Sandra Dallas*

## DRAWN & QUARTERED



## COMEBACKS

### DON'T GIVE UP THE SHIPYARD

THE U.S. COMMERCIAL SHIPBUILDING industry is sailing again. In 1993, American shipyards had no large, ocean-going vessels on order. But in 1994, there were 4; in 1995, 12.

Look at Tampa Shipyards, a unit of American Ship Building, once headed by New York Yankees owner George Steinbrenner. Recently, the shipyard court deal valued at more than \$20 million to Delphi American Maritime—part of Greek-owned Forum Maritime. Initially, Delphi plans

to do the heavy hull structuring in Eastern Europe and the more complex interior work in Tampa. In a few years, it wants to build ships at the Tampa yard.

With military orders and U.S. shipyards are recovering largely due to a federal loan guarantee program



IN TAMPA: Barge repair

panded in the Tampa yard doesn't use it, one example. At News, four dozen hull tankers are under construction for a Greek company, the first project to export in 35 years. Still, the U.S. industry has a long way to go. In gross tonnage last year, it placed 12th, behind Brazil. *Gail DeG...*

## THE BIG PICTURE

### SMALLER FOR ME, PLEASE

Hot-growth companies aren't as hungry for fresh capital. These fast-growing midsize outfits aim to raise less capital than last year for such things as plants and equipment. An exception: More companies plan to raise capital to buy another business.

REASONS FOR RAISING CAPITAL  
PERCENTAGE POINT CHANGE IN NUMBER OF MIDSIZE COMPANIES, 1994 VS. 1993



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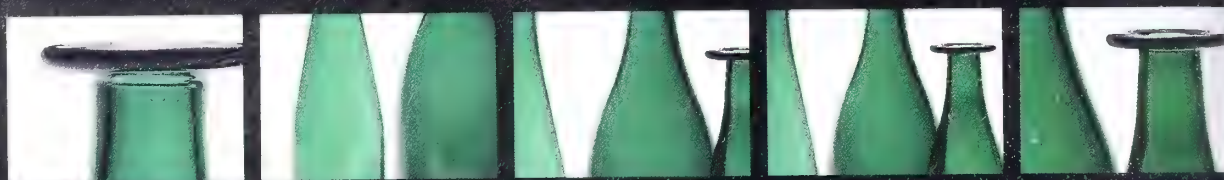
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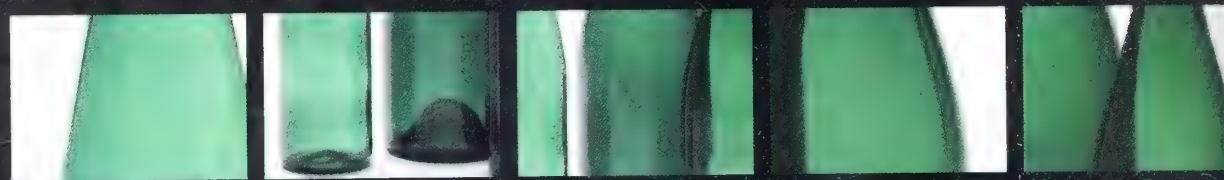




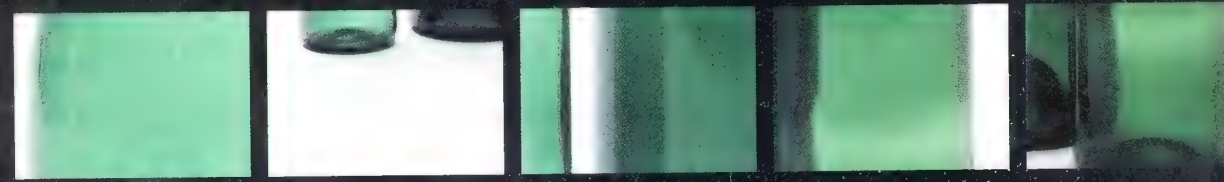
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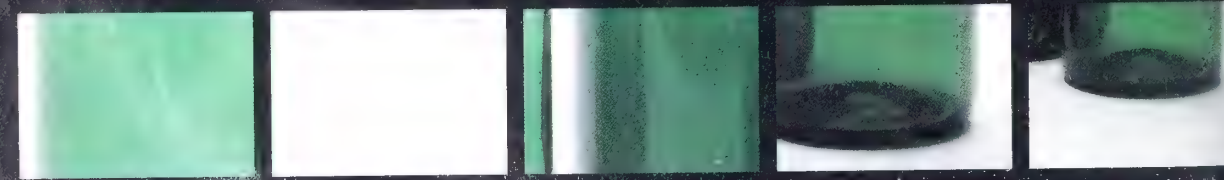
You need to locate a bottle design.



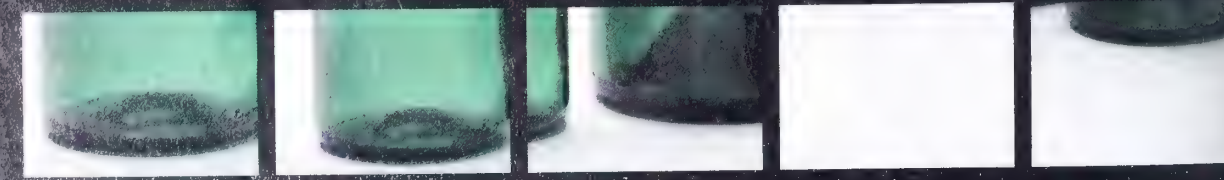
HQ's database has 40,000 bottles.



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## WHAT PRICE PRODUCTIVITY?

You just don't get it. Sure, the statistics in "Productivity to the rescue" (Cover Story, Oct. 9) bode well for the individual companies that are optimizing their use of technology. But even your own examples—of GTE Corp. in Tampa and DuPont Co.—remind us that today's steadily increasing productivity also implies a steadily decreasing need for labor.

The cumulative effect of this new automation is downright worrisome. In coming decades, businesses populated mainly by extremely productive robotic and "expert" systems will perform manufacturing and service work on a scale—and with social effects—that few people today are contemplating.

Yes, the production of goods and services may well be headed for the moon. But if only a smattering of paycheck-earning workers survives to consume them, so what?

Thomas Mulligan  
Brock University  
St. Catharines, Ont.

Your article failed to address one of the most important consequences of the productivity boom in America: rising stress levels and the deterioration of quality of life among overworked professionals, whose wage increases have barely (if at all) kept up with inflation. This degeneration, being a virtually immeasurable, intangible factor, is simply ignored by your cover story.

Marcelo Goulart  
Orlando

Although I am in general agreement that our nation's companies are gaining competitive ground, I think that some of the purported gains stemming from productivity increases are overstated.

First, the article states that "unit labor costs have been flat over the past year... a clear sign of improved efficiency." While the retardation of labor cost increases may in part stem from efficiency gains, I believe that the sup-

ply/demand relationship of labor is a contributing factor.

Second, the article states that the stock market's rise is powered by productivity, ostensibly through companies' greater earnings. While earnings have helped advance this market, I believe that many other factors, including liquidity, have played a greater role.

Finally, you credit "reengineering" for productivity boosts. While reengineering has been highly beneficial in many cases, in others it has served little more purpose than to cut expenses, including personnel, pay raises, R&D/new-product development, and investment. Although these cuts might add to short-term productivity, their benefit might well harm future prosperity.

Ted Kavadas  
Highland Park, Ill.

I found the article on productivity very encouraging and hopeful, although it does seem strange not to find one mention of the labor movement during the time period referenced. If recollection serves, a profound labor movement occurred during this period. This movement arose from the need to "persuade" business that gains in productivity should be shared.

I can only assume the authors, though not stating so, expect the same resurgence in labor will occur during this period of productivity expansion.

Russell E. Forte  
Glen Gardner, N.J.

## A GOLD STANDARD HAS SOME STERLING QUALITIES

Your article "The fake glitter of a gold standard" (News: Analysis & Commentary, Oct. 9) tries hard to discredit the idea of stabilizing the value of the dollar by tying it to a fixed measure such as gold. But the supposed disadvantages you cite—too simple, too rigid, too much oriented toward zero inflation—would be recognized by most people as virtues of a sound currency.

Not only would a gold-linked dollar restrict the ability of the Federal Re-

serve Board to manipulate the money supply for political ends but it would also permit the economy to grow at a dynamic pace in keeping with its inherent potential, rather than being held hostage by outdated academic notions of a "trade-off" between unemployment and inflation.

Jack Kemp, and now Steve Forbes, offer the right prescription for our economic anemia: We need to go back to the future with a gold standard.

Judy Shelton  
Marshall, Mo.

*Editor's note: Shelton is the author of Money Meltdown.*

## THERE'S NO SHORTAGE OF SKILLED AMERICANS

Your Commentary "How immigrants choke off growth" (News: Analysis & Commentary, Oct. 9) fails to account for the thousands of educated workers who have joined the ranks of the unemployed as a result of the restructuring that has taken place in America's high-tech industries. In addition, I think a check of U.S. colleges and universities will reveal that, compared to prior years, a far larger percentage of graduates now leave the institution without jobs or even job prospects.

I can't believe that Claremont Technology Group Inc. was unable to find need for 60 to 80 programmers within the U.S. I do believe that, like Hewlett-Packard Co. and other computer companies, it was lured by the low wages paid to high-tech workers in foreign countries.

Joseph Gendron  
East Granby, Conn.

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INSURANCE & INVESTMENT



BY STEPHEN H. WILDSTROM

## ENTERING A NEW DIMENSION

3-D will soon be the hottest thing to hit your PC, but don't be in too much of a hurry

If the notion of 3-D makes you think of wearing funny glasses at Walt Disney World, you're about to get a surprise. Technology that creates lifelike three-dimensional images is the most exciting new feature in personal computing. But if you rush to shell out \$250 to \$350 for the 3-D hardware-software packages that will hit the stores soon, be ready to do it over again in a year or so when some format conflicts get sorted out.

What is a 3-D display? Artists discovered how to create the illusion of depth on a flat surface 500 years ago. But no matter how realistic a 2-D rendering looks on the screen, it's still like a theater "flat"; if you look around the back, nothing is there. By contrast, a 3-D object is fully rounded. Rotate it on the screen and another side comes into view, with realistic contours and modeling of light and shadow.

**UPGRADE TIME.** Realism requires millions of computations, which has limited the production of 3-D graphics—for the movies, medicine, and other uses—to high-end workstations. Even today's speedy Pentiums can't do the job alone. Instead, they will rely on a new generation of display adapters, called 3-D accelerators. The new equipment will enable desktop computers to take a video im-

age and "map" it to fit a three-dimensional shape. One result: photorealistic animated figures instead of cartoons in computer games.

For most people, the initial uses of 3-D will be for games, and for the foreseeable future, creating those images will be the province of skilled computer programmers. Don't plan on playing these computer games on your old standby: At a minimum, Macintosh owners will need a machine with the new PowerPC chip, and Windows



fans will need a Pentium machine with Windows 95 and plenty of memory.

Spending \$1,500 to replace your 386 becomes even more intimidating when you realize that compatibility is not a high priority for developers of the new 3-D products. The manufacturers of new display adapters are pursuing different technologies, and software written for one won't work on any of the others.

Diamond Multimedia Systems Inc. is about to ship its Diamond Edge 3-D board in

October. The device, starting at around \$250, uses the NVIDIA NV1 chip. Creative Labs will be out in November with the \$350 3-D Blaster. At the heart of the Creative board is the new GLINT processor being developed by Creative and 3DLabs Inc. Early next year, Number Nine Visual Technology Corp. will ship a 3-D accelerator built around the Rendition Inc. Vérité chip. Similar products are in the works. All will include an assortment of multimedia games.

**QUICKDRAW.** Each of these companies is hoping to be the one that will define the 3-D graphics standard for Windows 95, and each company claims extensive support from major industry players. Unfortunately for consumers, this will probably mean a period of chaos. Something similar happened a few years ago when sound first appeared for PCs. Until Creative Lab's Sound Blaster emerged as the de facto standard, a sound-enhanced program might or might not work with a particular sound card.

In the Mac world, where Apple Computer Inc. controls the standards, things are much simpler. Apple's QuickDraw, a library of software routines that developers can use to create 3-D images on Power Macs, is available for free download on the Web (<http://www.apple.com>), along with demonstration software. Apple is counting on the PowerPC chip, rather than a graphics accelerator, to get 3-D images to the screen.

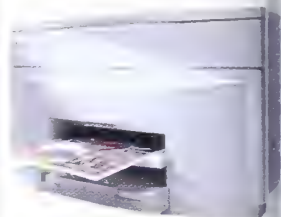
Hardware makers hope Microsoft Corp. will define a standard in a future version of Windows 95—and hope it will favor their technology. Hard-core gamers will want the latest technology as soon as it hits the stores. But most of us would probably do well to wait until a clear standard emerges. Remember Betamax vs. VHS?

## BULLETIN BOARD

### HARDWARE

#### COLOR COPIES R YOU

For most businesses, getting color copies used to mean either sending a job off to a corporate graphics or a trip to the nearest copy shop. But the new CopyJet from Hewlett-Packard Co. (800 752-0900), with retail prices beginning about \$2,500, makes color copying affordable for corpo-



rate departments and midsize businesses. The device doubles as a network color printer. The plain-paper ink-jet device turns out about one color page per minute as either a printer or a copier. The flatbed copier can handle reductions and enlargements from 50% to 400% and will print on pages up to legal size.

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ANY MAN  
se and Fall of Corporate Life  
hony Sampson  
Business • 354pp • \$27.50

# THE DINOSAUR IN THE RAY FLANNEL SUIT

mong chroniclers of the world's pillars of industry, few can match Anthony Sampson. The British dist's studies of the arms trade, industry's Seven Sisters, and ITT's world of corporate intrigue sit on bookshelf as classic histories to be read to time and again. Now, Sampson's turned his attention from the in-workings of specific corporations to the very culture of business.

*Company Man*, Sampson has pro-a social history of the men—and, onally, women—who inhabit the n corporation, from the 17th cen-adventurers of the British East Co. to the techies who sally forth icrosoft Corp. As the son of an ial Chemical Industries research ier who found fulfillment as a cog ast commercial engine, Sampson ses to a longtime fascination with iddle-class folk behind the facades porate giants. To Sampson, such onaries are not just "humanware" ide software and hardware." In-he sees them as individuals in nt conflict, caught between family isibilities and their need to keep ith corporate change.

only Sampson had fulfilled the se of his quest. For a complete ation of company man's evolution gh the ages, you would need a nation of Studs Terkel's keen ear al history and Vance Packard's eye for the passions and absur-of corporate life. But Sampson hort. He dutifully covers the pro-on of corporate governance from ctatorships of the 1920s to the s and high-tech entrepreneurs of n time. But except for during a our of Microsoft, he fails to dig e managerial implications of the information economy. And he s no new ground as he goes ove e of Japan Inc.'s competitive chal-

lenge. Rather than retelling the story of Toyota Motor Corp.'s ascendancy, it would perhaps have been better to detail the pain it caused in Detroit, where executives woke up in the 1970s and '80s to find themselves under siege.

I also wish Sampson had taken time to revisit *The Seven Sisters*, his 1975 treatment of Esso (now Exxon Corp.), Royal Dutch/Shell Group, and the other companies of the world oil cartel. It would have been instructive to examine the managerial stresses, strains, and triumphs as Big Oil plunged into an era of disastrous diversifications that eventually forced it to slim down and return to its basic task of searching for crude oil. But the closest that *Company Man* comes is to offer glimpses of Royal Dutch/Shell as it evolves from the dictatorship of Sir Henri Deterding in the 1920s and '30s to the postwar rule-by-committee norm.

To be sure, Sampson shows flashes of brilliance: His depiction of the intensely bureaucratic ICI, which in its glory years was a standard-bearer for the British Empire, is trenchant. Equally on target is his up-close description of the casual style and competitive spirit at Microsoft's campuslike headquarters in Redmond, Wash. "Bill Gates is more like a headmaster or supervisor than a tycoon," Sampson writes. "To be questioned by him is like a final university examination. But behind that discipline is the ultimate motivation of profit.... As I was told, 'It's like a return to raw 19th century capitalism.'" Except for one thing: Microsofties have a chance to apply entrepreneurial skills and earn big bucks through stock options.

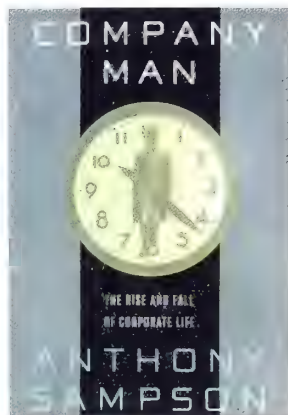
I wanted more of these penetrating observations to match the book's catchy title, itself a gentle play on *Organization Man*, William H. Whyte Jr.'s groundbreaking work on the insular conformity of U.S. corporate society during the Eisenhower era. Instead, what I got was material that treads familiar ground, often substituting observations of other authors and management consultants for the around-the-water-cooler chitchat that could have made Sampson's effort come alive.

At least Sampson picks up on Whyte's contention—proved all too true—that the inbred managers of America's postwar years were sowing the seeds of their own destruction. Indeed, that forms the basis of *Company Man*'s best moments. Sampson concludes that Whyte's organization men have been replaced, four decades later, by "disorganization men." This class of managers lives from restructuring to restructuring, as cost-cutting consultants squeeze out layers of fat and as instant global communication eliminates the need for lots of midlevel executives to handle the flow of information up and down corporate ranks.

"What had happened to the loyal old company men, the managerial class?" Sampson asks. "In the Sixties, they were the admired professionals, who had wrested power away from the owners of industry and built up the elaborate 'technostructure,' the great pyramids on which Western civilization depended. Yet by the late Eighties, they were facing purges in nearly all the big Western corporations...."

But should this development bring on mourning? Anything but. Today's restructurings are just another phase in the corporation's 400-year-long evolution. If anything, that process is speeding up. How company men and women meet the challenges of the Information Age will likely be the fodder for many more volumes. Some of them, I hope, will unlock the secrets of corporate life in livelier fashion.

BY WILLIAM GLASGALL  
Senior Writer Glasgow covers international finance and economics.



## AN INSIDE LOOK AT CORPORATE CULTURE—

## BUT SAMPSON'S GAZE ISN'T PENETRATING ENOUGH



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## HOT TYPE

Superinvestor George Soros last expounded on his theory of investing in 1987, with *The Alchemy of Finance*, which set forth the author's approach in sometimes painful detail. In *Underwriting Democracy and Opening the Soviet System*, he discussed his youth in Hungary and his revulsion for closed societies. Now comes *Soros on Soros: Staying Ahead of the Curve* (Wiley, \$19.95 paper, \$39.95 cloth), which is intended to update and fill in the gaps in the earlier works. It is written in a question-and-answer format, with queries posed by Morgan Stanley Group Inc. investment strategist Byron Wien and German journalist Krisztina Koenen.

At its best, *Soros on Soros* is chatty and moderately infor-

mative. The "interview" with Wien is the best part of the book, and it does a decent job of bringing us up to date. Soros gives his version of his troubled personal and professional relationships, including his breakup with early partner John Rogers. But there are still gaps: Not a word is said about Soros' recent and abortive real estate venture with Paul Paulson, the reclusive magnate.

Fully half the book treats Soros' favorite theme: the advantages of open over closed societies. Much of this is tedious and self-important, and not terribly original. But even though *Soros on Soros* isn't Soros at his best, the book has found a wide readership: It's the No. 3 paperback on this month's BUSINESS WEEK Best-Seller List.



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BY ROBERT KUTTNER

## WHY IS THE FED SO TERRIFIED OF GROWTH?



**EASE UP:**  
The more the economy becomes globalized, the more it can sustain higher growth and wages—without fear of inflation

**D**espite rising productivity, real living standards have been falling for most Americans. Much of this reflects structural changes in the economy—the shift to deregulation, globalization, and the weakening of unions—all of which reduce job security and labor bargaining power. The result is that the well-off capture the lion's share of economic gains.

But in 1994, according to the Census Bureau, a funny thing happened. Median family income, after falling for four straight years, actually rose by \$877, or 2.3%. In 1994, the economy did not become less global, or more regulated, or more unionized. So why did median incomes go up?

Easy. In 1994, the economy grew at a brisk 4.1%. This growth rate meant high job creation, which offset rising productivity and brought down the rate of unemployment. When the economy is growing rapidly and employers are adding new people, employees gain greater leverage to get their share of productivity gains—and the earnings of ordinary people go up.

But don't expect this trend to continue. The Federal Reserve thinks a 4.1% growth rate is dangerously high. This year, and for years to come, the Fed will target a real growth rate to around 2.5%. As long as this is the case, we can expect the broader structural trends to combine with sluggish growth to deny the average person increases in real living standards.

**SALARY HIKE.** This slow-growth consensus is beginning to erode, though the erosion is coming more from political forces than from the economics Establishment. Supply-siders, for example, have never bought what Robert L. Bartley once called the "root-canal" school of economics—the idea that economic virtue must be painful. Bartley's *Wall Street Journal* editorial page has continued to crusade for higher growth rates and has even given space to the Keynesian economist Robert Eisner, with whom Bartley agrees on little else.

In a recent essay, Professor Eisner pointed out that higher growth is associated with fuller employment and higher rates of productivity. When productivity rises, proportional wage increases are not inflationary. Hence high rates of growth and employment need not produce price increases and can actually counter inflationary pressures.

The prophets of slow growth ignore the

recent structural changes noted above, to alter the historic association of tight markets with inflation. In a global economy, U.S. workers think twice before pressing for wage hikes in excess of productivity gains. They risk pricing themselves out of the market. For a decade, the norm has been for median wage growth to lag behind productivity growth, in boom years as well as recession years. Sellers are likewise restrained from extracting price increases by the proliferation of competitors. The more the economy becomes deregulated and globalized, the more it can sustain higher growth rates without courting inflation. Somebody should tell the Greenspan.

**WALL STREET TALKS.** Last month, the National Association of Manufacturers, not exactly a temple of Keynesian economics, issued a tough statement calling for a target growth range of 3% to 3.5%. (BUSINESS WEEK concurs; see its Oct. 9 editorial.) It is a big moment in political economy when the NAM thinks the economy can prudently grow at 3.5% and a Democratic Administration (even by the Fed) gratefully settles for 2.5%.

This is an old story—Main Street vs. Wall Street. The real economy is capable of high growth and fuller employment. This is vividly true in the 1990s, given the combination of computerization, higher productivity, global competition, and disciplined labor markets. But the financial economy, to which the Fed responds, is more concerned about the volatility of the bond market and associates slow growth with financial soundness.

Economists debate the relative roles of macroeconomics as well as microeconomic interventions such as education, training, technology, and labor policy in raising living standards. Micro measures have their place, but the growth rate is the cake and mostly the frosting. When the economy grows at 4%, jobs are plentiful, labor has bargaining power, and wages can rise with productivity. In that context, it pays for companies to spend on training to upgrade skills and to prevent worker shortages. But when growth is 2%, spending on human capital may not compensate corporations sufficiently and may yield an overeducated, underpaid, frustrated workforce. The preconditions are in place for a new era of rising growth and broadly distributed prosperity. The Fed should take its miserly foot off the brake.

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BY GENE KORETZ

## MONETARY DATA POSE A RIDDLE...

M2 is surging, M1 is way down

It wasn't that long ago that the financial markets awaited news of money-supply growth with bated breath. But the erratic relationship between various monetary measures and the economy has tempered market concerns.

Still, as economist David H. Resler of Nomura Securities International Inc. points out: "The current monetary picture is somewhat disquieting." On the one hand, M2, the most closely watched monetary aggregate, has recently begun to grow at a hefty 7% annual rate, pointing to a resurgent economy. On the other, M1, the narrow money supply, has just posted its fifth straight month of negative 12-month growth—foretelling a deepening threat of recession.

The problem is that though M2 is supposed to be more reliable than M1 as a leading indicator, it is M1 that has had a better track record over the past six or seven years. Its growth accu-

uncanny parallels to 1988-1989," says Resler, "both the markets and the Fed would be well advised to pay closer heed to the nearly identical behavior of M1 and M2 in recent months to their movements six years ago."

## ...DO RUSSIANS HOLD THE KEY?

They're wary of holding greenbacks

Despite the parallels to the past, some money market mavens are unfazed by M1's current weakness. They believe two new developments are distorting its growth on the downside.

The first is the growing practice among banks of sweeping funds from interest-bearing checking accounts, which are part of M1, into savings deposits, which are part of M2. Because savings deposits, unlike checking accounts, aren't subject to the Fed's reserve requirements, such sweeps enable banks to enhance their supply of loanable funds (unencumbered by reserve requirements) without hurting consumer access to checking accounts.

The second development involves Russian demand for U.S. currency. Over half of greenbacks in circulation are held outside the U.S., and Russia's stock of dollars may run as high as \$30 billion (including several billion in counterfeit \$100 bills). Economist David Hale of Kemper Financial Services Inc. notes that a more stable ruble combined with fears about U.S. plans to issue a new counterfeit-proof \$100 bill have sharply cut Russian demand for dollars. Because the Russian government in the past has declared existing bank notes to be worthless, he says, many Russians are now wary of old \$100 bills.

The bottom line: The popularity of "sweep accounts" and Russians' current aversion to U.S. currency are undoubtedly helping to keep M1 down. But if it stays down much longer, recessionary fears will inevitably grow.

## SUPERWOMAN? GOOD LUCK

Not many have kids and a career

rately foreshadowed not only the last recession and subsequent recovery but also the economy's acceleration last year and more recent slowdown (chart).

Indeed, as Resler notes, the current monetary pattern bears a striking resemblance to the situation six years ago. In mid-1989, M2 growth accelerated dramatically, hitting a 7%-plus annual rate for five straight months. Meanwhile, M1 remained stalled below year-earlier levels for four months. The behavior of M2, of course, implied quickening economic growth and inflationary pressures ahead, but it was M1's warning of a possible recession down the road that was confirmed by the contraction of mid-1990.

"Facing an economy already rife with

U.S. college graduates had great success in achieving those twin goals.

Goldin looked at four "cohorts" of white women college grads in this century. She found that while half of the graduating around 1910 turned out childless, their counterparts in the 1930s tended to raise families and working for awhile upon graduation. In contrast, the postwar women graduates the mid-1950s tended to stress marriage and children first and then to join the labor force, often as teachers.

It's the last crop of college graduates who received their degrees in the late 1960s through late 1970s, who are closest in their aspirations to today's college women. By 1991, when the group was 37 to 47 years old, Goldin found that only 24% to 33% had achieved a career—defined as holding a full-time job that pay above the lowest 25% of comparable male graduates. What's more, half of these career women (and 28% of the entire group) were still childless.

Thus, notes Goldin, "by the time they were about 40 years old, relatively few members of this group had successfully combined children and a career." But today's women graduates do better

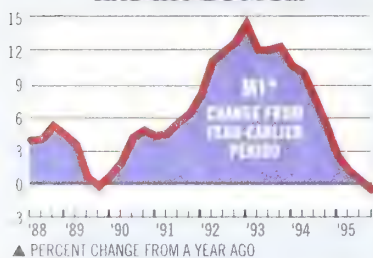
## A TIDAL WAVE OF MARKS

Cross-border investment is soaring

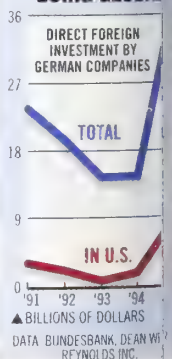
Just how bad have the strong marks and Germany's high wages been for German industry? Bad enough to spark a massive surge in direct foreign investment. Measured in marks, cross-border investment is running at double last year's pace, and in dollars, economist Joseph P. Quinlan of Dean Witter Reynolds Inc. says this year's total will hit a record \$37 billion (chart).

Interestingly enough, while German direct investment in Asia is exploding, about two-thirds of this year's outflow is going to Britain, France, and the U.S., which is enjoying a hefty increase in dollar terms. "German industry, fearful of currency volatility, wants a bigger stake in its major markets," says Quinlan.

### THE BASIC MONEY SUPPLY HAS HIT BOTTOM



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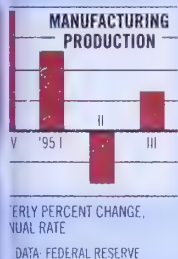
MES C. COOPER & KATHLEEN MADIGAN

## THE FED'S SOFT LANDING HAS ROOM TO GLIDE

### U.S. ECONOMY

In the 1972 movie *The Candidate*, Robert Redford sells his way to win an election. In victory, he turns to his hand and says simply, "Now what?" You could ask the Federal Reserve the same question about the economy. The Fed-engineered "soft landing" is here. By keeping interest rates relatively high, the central bank has slowed the economy enough to create some industrial slack and short-circuited inflationary pressures. Even under the tight monetary reins, the expansion shows no signs of stumbling into recession.

### FACTORY OUTPUT IS STARTING TO PICK UP



The latest data show more evidence of the soft landing. Retail sales are rising modestly. Factory output has bounced back (chart), and inventory growth has slowed. Inflation, meanwhile, isn't even in gear—it may even be in reverse—partly because some of the rise in domestic demand is being satisfied cheaply by imports and partly because of in-conscious consumers.

So, now what? By all indications, the Fed seems content with the status quo. And given the higher productivity and the absence of cost pressures, policymakers may tolerate growth somewhere between 2½% and 3%, at an annual rate, over the next quarters, without worrying too much about inflation. Recent reports suggest that is where the economy has ended.

Not for the 1996 budget, now under hot debate, the Fed might be inclined to keep policy on hold for a while.

But if Washington delivers a credible package of tax reduction, the Fed seems ready to offset the negative fiscal drag with a cut in interest rates.

### BEST CLUE

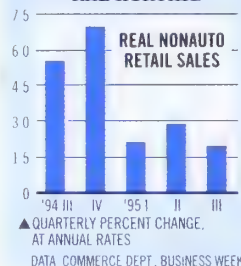
to the economy's health is the out-of-pocket consumer spending, especially during the crucial holiday season. Thanks to decent, if slower, growth in wages and incomes this year vs. last, consumers have more resources to lift their purchases of goods and services. A quarter close to the 3% to 3½% annual rate was hit in the third quarter. But while shoppers will be busy in the holiday season, profit-starved retailers may be in the good cheer amid the need to discount. Retail sales were in good shape in September. Total sales rose 0.3%, and excluding weak car buying, they were up 0.7%. In fact, except for car dealers and

restaurants, all the major categories posted solid sales gains last month.

For the third quarter, real retail sales grew at a 4% annual rate, thanks to strong car buying earlier in the summer. Nonauto receipts rose at a 2% rate. While respectable, the pace was below the 2.9% gain in the spring (chart). And it came at a cost to retailers.

That's because consumers required price cuts to crack open their wallets, and those sales promotions are ruining retailers' profits. Heavy discounting forced Kmart Corp. to report that its third-quarter profits will be below year-ago levels—leading to speculation that the retailer would file for bankruptcy. Chrysler Corp. had to boost its rebates by a huge \$350 per vehicle. That was partly responsible for the 46% plunge in Chrysler's earnings.

### WHY SOME RETAILERS ARE HURTING



Discounting is a key reason for low inflation. In September, consumer prices inched up 0.1%. Excluding food and energy, core prices increased just 0.2%. Producer prices of finished goods rose 0.3% last month—the first gain since May—while core producer prices rose 0.2%. Consumer inflation is on track to end the year below 3%. If so, 1995 would be the fourth straight year of sub-3% inflation; 1996 may well be the fifth.

Consumer prices for goods alone edged up at an annual rate of just 0.6% in the third quarter, and they fell excluding food. As usual, the bargain hunting will grow even more intense during the holiday season. So retailers will struggle to maintain profit margins, and inflation will remain inconsequential.

Low inflation coupled with faster growth in nominal wages means that real hourly pay is finally increasing. This gain in purchasing power, evident in the third quarter's solid advance in real aftertax income, is another reason to expect consumer demand to hold up.

### FOREIGN DEMAND

looks buoyant as well. Exports of goods and services in August jumped 3.7% to a record \$65.7 billion, led by autos, aircraft, and high-tech equipment. Because imports were flat, the trade deficit shrank sharply, from \$11.2 billion to \$8.8 billion, the smallest gap of the year.

The August improvement implies that net trade was much less of a drag on third-quarter economic growth than had been anticipated. The month's surge in exports



suggests that U.S. manufacturers are benefitting from better growth abroad.

Steady growth in overall demand will support a continued pickup in industrial production in the fourth quarter. Industrial output fell 0.2% in September, but the decline mainly reflected a steep 5.4% plunge in utility output after the summer's hot weather boosted output to an unusually high level.

In the manufacturing sector alone, September output rose 0.2%, following a strong 0.9% advance in August. Those gains were the first since January.

Manufacturing output rose at an annual rate of 2.5% last quarter, after a second-quarter drop, but hours worked in the factory sector fell 2.7%. That combination suggests another excellent quarterly gain in factory productivity that will restrain unit labor costs and lift profits. BUSINESS WEEK's early-bird tally shows overall corporate profits up last quarter but at a slower pace than in the first half (page 36).

**LEADING THE OUTPUT PICKUP:** consumer durables, business equipment, and construction supplies. Cars and trucks strengthened, as did home-related durables. Business equipment is fueled by information processing, with computer and office items up 26.9%. Better housing demand is lifting construction supplies.

The production rebound is a sign that businesses have cleared out most of their excess inventories that

had cropped up earlier in the year. Inventory growth in manufacturing, wholesaling, and retailing has slowing steadily all year, and stock levels rose 0.4% in August. And because of a strong 1.5% increase in business sales, the ratio of stocks to sales fell sharply. Manufacturing inventories, about half the total, did not rise at all for the first time in a year.

One disturbing sign was a sharp 1% increase in retail inventories in August (chart). However, that rise was concentrated in furniture, building materials, and food, areas where the buildups were probably intended, especially in light of the strength in housing demand. With excess inventories about gone, the way is clear for further output gains—and continued expansion.

Of course, the longer you try to balance growth and inflation, the harder it is to maintain equilibrium. The danger is that the expansion could pick up steam and barrel through 1996, stoking price pressures. Conversely, the worrisome buildup in consumer credit and big cuts in government spending could send the economy into a tailspin. For now though, steady noninflationary growth is the best bet.



## BRITAIN

# INFLATION: ANOTHER HEADACHE FOR THE TORIES

A mix of slower growth and rising inflation comes at a bad time for Prime Minister John Major's Conservative government. Running some 30 points behind the Labor Party in the polls, the Tories are looking to stimulate the economy. The problem: Faster inflation may preclude an interest rate cut, and it reduces the leeway for a tax cut.

The retail price index jumped 0.5% in September, bringing the headline inflation rate to a three-year high of 3.9%. Underlying inflation, excluding mortgage interest, hit 3.1%, and the Bank of England's pet measure, the RPI excluding mortgages and certain taxes, is also increasing (chart).



The September RPI hardens the BOE's view that cost pressures are pushing their way forward and that retailers are regaining some pricing power. September prices at the factory gate, excluding food and energy, were up 5.1% annually, a four-year high. The government's target for underlying retail inflation is 2.5%, but analysts believe that goal is unattainable in 1996, without interest rate hikes, which Chancellor of the Exchequer Kenneth

Clarke opposes.

However, a slower economy will keep inflation from getting out of hand. Retail sales were flat in September and were down 0.4% from a year ago, the first annual

decline since July, 1992. That weakness, plus the slowing trend in industrial production, suggests third-quarter real gross domestic product grew no faster than its modest 2.3% pace in the first half. A continued drawdown of excessive inventories will keep fourth-quarter growth subdued as well, say analysts.

Major and Clarke strongly implied at the Conservative Party conference in Blackpool that the Nov. 28 budget would contain tax cuts. Major also promised to hold public spending to 40% of GDP, from 42.5% now. However, faster inflation will lift government outlays on social programs in 1996. Moreover, this year's budget is already overshooting its target, as sluggish growth eats into tax revenues, and as outlays outstrip last year's projections.



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## FUND-RAISING

# PUTTING THE BITE ON CORPORATE AMERICA

For the Presidential pack, the fund-raising is feverish

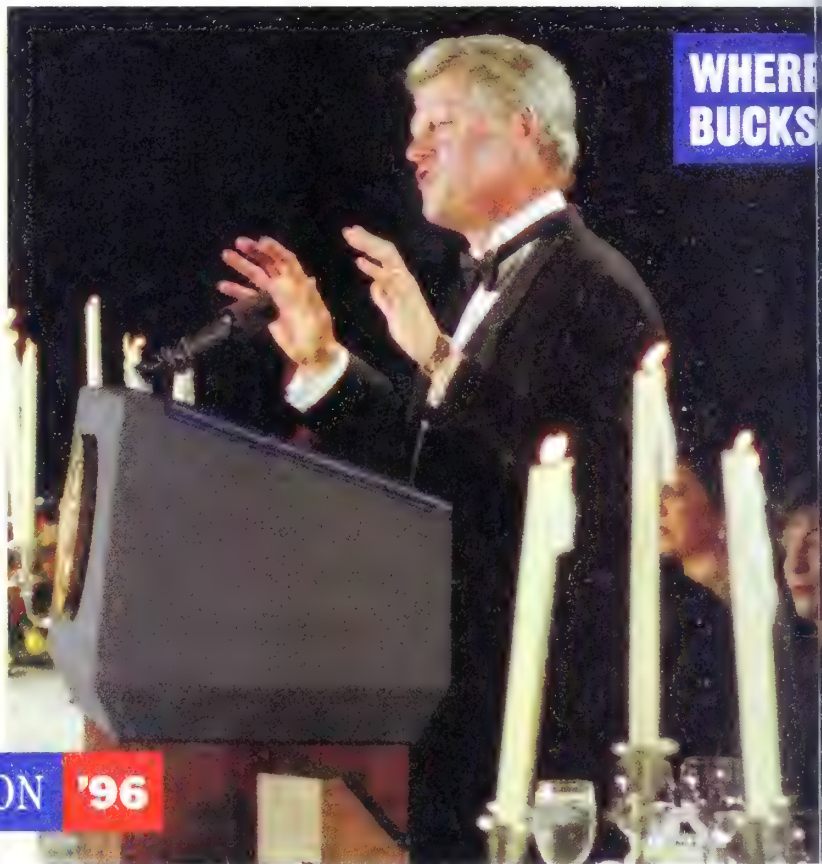
The chandeliers twinkled at the Sheraton New York as 1,000 business executives and politicians dined on lobster medallions and filet mignon. Donald Trump was working the room. But it was The Bob that folks had come to see. That's Senator Bob Dole of Kansas, the headliner at the \$1,000-a-head event on Oct. 16. "Now, I'm not here to pick a fight with President Clinton," he deadpanned. "It would be no contest."

The crowd roared at that. For the most part, though, this was a pretty jaded group. Through most of Dole's speech, forks clanked and table talk continued. "They're all the same—rubber-chicken dinners," shrugged one bored participant.

No matter—his wallet was still open, as are many others at hundreds of similarly tiresome fund-raisers across the nation. Whether it's Dole on the dais, or Senator Phil Gramm of Texas or former Tennessee Governor Lamar Alexander or Senator Richard G. Lugar of Indiana, the 1996 GOP Presidential money sweepstakes is in full throttle. And "it's the most feverish fund-raising effort I've ever seen," says John M. Hennessy, CEO of CS First Boston, who has raised money for both Gramm and Alexander.

**EARLY CONTESTS.** In the first nine months of the year, the 10 contenders for the GOP nomination have raised a record \$53 million, according to campaign accounts filed Oct. 16 with the Federal Election Commission. That's more than both parties combined had raised at this point in the last Presidential election campaign. Leading the pack is Dole, with \$18.8 million, followed by Gramm's \$14.3 million. None have caught President Clinton, who has socked away \$19.8 million, plus \$1 million more from events in Dallas on Oct. 16 and Houston on Oct. 17.

Each GOP candidate has a corporate



**HAIL TO THE CEOs:** Clinton woos executives at a Business Council dinner

niche. Although strong in every region and industry, Senate Majority Leader Dole is raising huge sums from insurance, gambling, and telecommunications companies—all with business before Congress. Gramm has called on oil and gas pals in Texas, and is popular with small business. Alexander and Lugar have targeted entrepreneurs. And though Patrick Buchanan's protectionist message turns off most execs, it's luring cash from some textile interests. "I admire his concern that we're losing

the middle class in this country," says CEO Roger Milliken of Milliken & Co.

Never has the need for early action been so great. In past campaigns, candidates raised funds for the New Hampshire primary, hoping a good showing would attract funds for later contests. At this time four years ago, Democratic contenders had raised just \$2.2 million. But in 1996, 70% of the delegates will be chosen within six weeks of the Hampshire. GOP contenders must raise money now for these pivotal contests.



all the wooing of Corporate America, though, there's disquiet in CEO-land. Some Dole backers fret that he's low on the buzz (page 53). Other executives retired General Colin L. Powell. Kenneth L. Lay, chairman and CEO of Enron Corp., is a Gramm fund-raiser. Says Powell has "great integrity. I like to see him run." Silicon Valley executives are wavering, too. High-tech was key to Clinton's 1992 success, but many CEOs are disappointed in him and with California Governor Pete Wilson out of the race, they're not lined up with the GOP field. "There is no one I'm excited about," says Michael J. Ellison, CEO of Oracle Corp. Others aside, Dole still has signed up

that Dole will look out for its interests. Many gaming executives supported Clinton in 1992. That was before he flirted with imposing a 4% tax on gross casino receipts to finance welfare reform. The industry now sees Dole as the one most likely to beat Clinton. So last June, Stephen A. Wynn, CEO of Mirage Resorts Inc., hosted a Las Vegas event that raised \$500,000 on his behalf.

**FALTERING MACHINE.** Gramm's support is more regional. About 48% of the money he raised in the first half of the year came from Texas, according to the Center for Responsive Politics. His support for tax breaks and regulatory relief for oil and gas companies has won the allegiance of industry executives. Says Enron's

know the fund-raiser and are coming to meet Lamar." The Tennessean's campaign is targeting entrepreneurs by pitching Alexander's own experience as co-founder of a company that helps businesses set up child-care centers.

Lugar, too, has had a hard time broadening his appeal beyond home. Many donors work for Indiana companies such as Eli Lilly & Co., whose CEO, Randall L. Tobias, and other executives have given to their favorite son. As chairman of the Senate Agriculture Committee, Lugar appeals to food executives such as William D. Smithburg, CEO of Chicago-based Quaker Oats Co. And childhood chum William D. Ruckelshaus, now chairman of Brown-Forman Industries Inc., will soon host

## CLINTON

**AMOUNT RAISED** **\$19.8 million**

Michelle, CEO, Equitable; Howard, CEO, Loral; Hoffman Jr., CEO, Seagram. Clinton may personally support the incumbent, but the incumbent has had little trouble in business to write checks.

**AMOUNT RAISED** **\$18.8 million**

### DONORS

Drew Lewis, CEO, Union Pacific; Boone Pickens, CEO, Mesa; Stephen Wynn, CEO, Mirage Resorts

Support comes from large corporations in a number of industries and regions, including telecommunications, and gambling.

## PHIL GRAMM

**AMOUNT RAISED** **\$14.3 million**



### DONORS

Harvey Golub, CEO, American Express; Kenneth Lay, CEO, Enron; John Stafford, CEO, American Home Products

Independent oil and gas producers in native Texas are fans, as are lumber companies, health-systems businesses, and small-business executives.

## LAMAR ALEXANDER

**AMOUNT RAISED** **\$8.6 million**



### DONORS

Stewart Turley, CEO, Eckerd; Stephen Lynn, CEO, Shoney's; Ray Irani, CEO, Occidental Petroleum

Expanding fund-raising from home state of Tennessee, with emphasis on entrepreneurs.

## PATRICK BUCHANAN

**AMOUNT RAISED** **\$4.3 million**



### DONORS

Roger Milliken, CEO, Milliken & Co.; Thomas Monaghan, CEO, Domino's Pizza; John Breen, CEO, Sherwin-Williams

Has raised some corporate money from textile executives, who like his protectionist platform.

## RICHARD LUGAR

**AMOUNT RAISED** **\$3.8 million**



### DONORS

Donald Fites, CEO, Caterpillar; William Smithburg, CEO, Quaker Oats; Randall Tobias, CEO, Eli Lilly

The chairman of the Senate Agriculture Committee has raised most of his money from Indiana and Illinois businesses, some in food industries.

most high-profile endorsements. Among his big donors: the Baby Bells, who have won his support on a bill that would make it easier for them to offer long-distance service. BellSouth Corp. John L. Clendenin headed a Dole fund-raiser in Atlanta that raked in \$100,000—and FEC records show that BellSouth employees wrote campaign checks. Clendenin says his position on the telecom bill was the reason for his support: "I happen to think Bob Dole would be the best Republican candidate."

Lay: "He's pro-free trade, pro-investment, good on downsizing government. He has so many positions that line up with the business community." But Gramm's money machine faltered in the third quarter, in part because he had a hard time lighting fires outside his base. "He's a hard sell north of the Mason-Dixon line," says one CEO.

For those without name recognition, raising money is a grind. Says Mel Sembler, an Alexander fund-raiser and Florida shopping-center developer: "Major contributors are either giving to Lamar because they know him or because they

know the fund-raiser and are coming to meet Lamar." The Tennessean's campaign is targeting entrepreneurs by pitching Alexander's own experience as co-founder of a company that helps businesses set up child-care centers.

With only four months before New Hampshire, all the candidates will be scouring the country for holdouts. With so much at stake, the hunt for dollars won't let up until every lobster medallion is devoured and the last ice swan is but a puddle on the ballroom floor.

By Susan B. Garland in Washington, with Oluwabunmi O. Shabi in New York, Mike McNamee in Williamsburg, Va., and bureau reports

FEDERAL ELECTION COMMISSION, BUSINESS WEEK



## CORPORATE PROFITS

# A STRONG, IF UNEVEN, THIRD QUARTER

Technology was the star, while autos underachieved

**B**USINESS WEEK's flash report on third-quarter results signals that the fat lady hasn't sung for this earnings boom. Profits were up only 11% on a 10% revenue increase, down from a 45% hike last year on a 10% sales gain. But take out IBM (and the \$1.8 billion charge related to its Lotus acquisition), and earnings jumped 18% overall. Another good sign: per-share numbers came in 4¢ higher than midquarter estimates. IBM and Apple aside, tech was a star performer, led by Intel's 41% jump and Microsoft's 58% gain. Among under-achievers: the auto biz, because of declines at Ford (-68%) and Chrysler (-46%). Both have new models coming on line, so results should pick up.

*Frederick F. Jespersen*



CURRENT QTR. SALES (MILLION)

| INDUSTRIALS             |          | 199 3Q7 1 |
|-------------------------|----------|-----------|
| ALCOA                   | 3,264.8  |           |
| ALUMAX                  | 767.7    |           |
| ARCO CHEMICAL           | 999.0    |           |
| BAUSCH & LOMB           | 476.8    |           |
| CATERPILLAR             | 3,733.0  |           |
| CHAMPION INTERNATIONAL  | 1,840.7  |           |
| CHRYSLER                | 12,009.0 |           |
| CONAGRA                 | 6,436.4  |           |
| CORNING                 | 1,568.8  |           |
| CPC INTERNATIONAL       | 2,046.2  |           |
| CUMMINS ENGINE          | 1,219.0  |           |
| DANA                    | 1,727.1  |           |
| EASTMAN KODAK           | 3,813.0  |           |
| FORD MOTOR              | 31,418.0 |           |
| GENERAL ELECTRIC        | 17,341.0 |           |
| GENERAL MOTORS          | 37,462.9 |           |
| GEORGIA-PACIFIC         | 3,705.0  |           |
| HARLEY-DAVIDSON         | 427.0    |           |
| INLAND STEEL            | 1,128.5  |           |
| INTERNATIONAL PAPER     | 5,100.0  |           |
| JOHNSON & JOHNSON       | 4,738.0  |           |
| LILLY (ELI)             | 1,631.9  |           |
| MATTEL                  | 1,176.5  |           |
| MCDONNELL DOUGLAS       | 3,346.0  |           |
| MERCK                   | 4,171.1  |           |
| OWENS-CORNING FIBERGLAS | 927.0    |           |
| PEPSICO                 | 7,693.1  |           |
| PFIZER                  | 2,624.3  |           |
| PHILIP MORRIS           | 16,689.0 |           |
| REYNOLDS METALS         | 1,841.0  |           |
| RUBBERMAID              | 641.5    |           |
| SCOTT PAPER             | 1,093.4  |           |
| SHERWIN-WILLIAMS        | 911.4    |           |
| UNION CAMP              | 1,073.5  |           |
| WEYERHAEUSER            | 3,111.6  |           |
| WHIRLPOOL               | 2,154.0  |           |
| SERVICES                |          | 38,428.2  |
| AMR                     | 4,445.0  |           |
| BANKAMERICA             | NA       |           |
| BEAR STEARNS†           | 1,074.4  |           |
| CBS                     | 725.2    |           |
| CHASE MANHATTAN         | NA       |           |
| CHEMICAL BANKING        | NA       |           |
| CITICORP                | NA       |           |

## CORPORATE PROFITS

## ALOFT AT MICROSOFT

Great results. But how long can it ride high on Win95?

**T**he high-tech jitters may be gone, for now. But the buzz isn't going away. On Oct. 17, Microsoft Corp. announced quarterly earnings that showed an eye-popping 7 million copies of Windows 95 were sold to customers.

That boosted revenues and earnings to record levels. But it hasn't prevented all the talk: Are Win95 sales slowing down? Are retailers sitting on a mountain of unsold inventory? Says analyst Rick G. Sherlund of Goldman, Sachs & Co.: "It was a terrific quarter, but the critical issue is, what is the current sell-through rate?"

No argument on the great quarter. Microsoft reported a 62% jump in revenues, to \$2.02 billion. Earnings rose 58%, to \$499 million, or 78¢ a share, a big leap over the expected 68¢. Euphoric investors sent the stock flying high: up 4.5 points, to close at 95½ on Oct. 18. That's a big turnabout from re-

cent weeks, when inventory worries sent the stock skidding from \$90 to Aug. 24—the day Win95 was launched—to \$81 a week ago.

Was there cause to worry? Clearly there was no inventory glitch in the quarter just ended. Microsoft's revenues and earnings are based on what is sold through to customers, not to retailers. What's more, independent market researcher PC Data confirms what Microsoft sold into the retail channel and one step further: Of all the software sold in September, 25% of it was either Windows 95 or Windows 95 applications programs.

But is there a problem going on

| RG. | EST. EPS<br>(8/17) | REPORTED<br>EPS | DIFF. |                        | CURRENT QTR. SALES<br>(MILLIONS) | % CHG. | QTR. PROFITS<br>(MILLIONS) | % CHG. | EST. EPS<br>(8/17) | REPORTED<br>EPS | DIFF. |
|-----|--------------------|-----------------|-------|------------------------|----------------------------------|--------|----------------------------|--------|--------------------|-----------------|-------|
| 13  | 0.90               | 0.92            | +0.02 | ENRON                  | 2,200.0                          | +8     | 100.6                      | +5     | 0.41               | 0.40            | -0.01 |
| 23  | 1.10               | 1.27            | +0.17 | FEDERAL EXPRESS        | 2,453.4                          | +10    | 75.3                       | +23    | 1.15               | 1.33            | +0.18 |
| 26  | 0.83               | 0.90            | +0.07 | FIRST CHICAGO          | NA                               | NA     | 207.2                      | +35    | 1.70               | 2.12            | +0.42 |
| 14  | 1.43               | 1.21            | -0.22 | FOOD LION              | 1,914.0                          | +3     | 41.0                       | +12    | 0.09               | 0.09            | —     |
| 36  | 0.81               | 0.75            | -0.06 | GANNETT                | 932.3                            | 0      | 96.1                       | -9     | 0.79               | 0.69            | -0.10 |
| 13  | 1.30               | 1.07            | -0.23 | MARRIOTT INTERNATIONAL | 1,926.0                          | +6     | 46.0                       | +24    | 0.35               | 0.35            | —     |
| 19  | 2.17               | 2.44            | +0.27 | McGRAW-HILL            | 904.4                            | +6     | 105.8                      | +17    | 2.11               | 2.12            | +0.01 |
| 16  | 1.03               | 0.90*           | -0.13 | MERRILL LYNCH          | 5,431.1                          | +20    | 300.4                      | +30    | 1.39               | 1.47            | +0.08 |
| 13  | 0.35               | 0.36            | +0.01 | MORGAN (J.P.)          | NA                               | NA     | 360.0                      | +10    | 1.57               | 1.78            | +0.21 |
| 9   | 0.59               | 0.37            | -0.22 | NATIONSBANK            | NA                               | NA     | 530.0                      | +23    | 1.74               | 1.93            | +0.19 |
| 13  | 0.95               | 0.95            | —     | OFFICE DEPOT           | 1,337.1                          | +28    | 36.8                       | +34    | 0.24               | 0.24            | —     |
| 26  | 1.35               | 1.14            | -0.21 | PAINEWEBBER GROUP      | 1,379.6                          | +47    | 78.2                       | +284   | 0.35               | 0.67            | +0.32 |
| 15  | 0.60               | 0.60            | —     | ROADWAY SERVICES       | 1,108.4                          | +2     | 2.3                        | -80    | 0.34               | 0.06            | -0.28 |
| 15  | 0.95               | 0.99            | +0.04 | SAFEWAY                | 3,845.5                          | +6     | 83.7                       | +31    | 0.64               | 0.69            | +0.05 |
| 18  | 0.44               | 0.27            | -0.17 | SCHWAB (CHARLES)       | 385.5                            | +55    | 47.2                       | +51    | 0.25               | 0.26            | +0.01 |
| 11  | 0.96               | 0.96            | —     | TIME WARNER            | 1,981.0                          | +5     | -102.0                     | NM     | -0.11              | -0.30           | -0.19 |
| 16  | 0.38               | 0.42            | +0.04 | TRAVELERS GROUP        | 4,511.8                          | -4     | 481.4                      | +45    | 1.14               | 1.45            | +0.31 |
| 12  | 3.37               | 3.57            | +0.20 | USAIR                  | 1,873.4                          | +7     | 43.1                       | NM     | -0.96              | 0.35            | +1.31 |
| 0   | 0.37               | 0.32            | -0.05 | WELLS FARGO            | NA                               | NA     | 261.0                      | +20    | 4.55               | 5.23            | +0.68 |
| 15  | 0.74               | 0.33            | -0.41 | TECHNOLOGY             | 41,537.1                         | +20    | 2,432.6                    | -19    | 1.15               | 1.10            | -0.05 |
| 16  | 1.37               | 1.27            | -0.10 | ADVANCED MICRO DEVICES | 590.4                            | +9     | 56.2                       | -35    | 0.87               | 0.52            | -0.35 |
| 19  | 0.94               | 0.96            | +0.02 | APPLE COMPUTER††       | 3,003.0                          | +20    | 60.0                       | -48    | 1.04               | 0.48            | -0.56 |
| 5   | 1.10               | 1.08            | -0.02 | COMPAQ COMPUTER        | 3,594.0                          | +27    | 245.0                      | +22    | 0.94               | 0.89            | -0.05 |
| 15  | 0.69               | 0.67            | -0.02 | HONEYWELL              | 1,680.3                          | +11    | 84.2                       | +21    | 0.63               | 0.66            | +0.03 |
| 9   | 1.53               | 1.70            | +0.17 | IBM                    | 16,754.0                         | +9     | -538.0                     | NM     | 2.54               | 2.30*           | -0.24 |
| 0   | 0.70               | 0.70            | —     | INTEL                  | 4,171.0                          | +46    | 931.0                      | +41    | 1.05               | 1.05            | —     |
| 12  | 1.23               | 1.28            | +0.05 | MICROSOFT†             | 2,016.0                          | +62    | 499.0                      | +58    | 0.68               | 0.78            | +0.10 |
| 4   | 0.75               | 0.77            | +0.02 | MOTOROLA               | 6,851.0                          | +21    | 496.0                      | +31    | 0.82               | 0.81            | -0.01 |
| 16  | 0.65               | 0.67            | +0.02 | POLAROID               | 580.0                            | +1     | 23.7                       | -19    | 0.84               | 0.51            | -0.33 |
| 7   | 1.69               | 1.71            | +0.02 | RAYTHEON               | 3,153.0                          | +29    | 200.7                      | +5     | 1.66               | 1.65            | -0.01 |
| 11  | 1.42               | 1.56            | +0.14 | SUN MICROSYSTEMS       | 1,485.3                          | +17    | 84.7                       | +120   | 0.65               | 0.85            | +0.20 |
| 15  | 0.37               | 0.32            | -0.05 | SYBASE                 | 233.1                            | +7     | 1.1                        | -95    | 0.16               | 0.02            | -0.14 |
| 15  | 0.81               | 1.02            | +0.21 | TEXAS INSTRUMENTS      | 3,426.0                          | +33    | 289.0                      | +56    | 1.44               | 1.48*           | +0.04 |
| 5   | 0.89               | 0.87            | -0.02 | UTILITIES & TELECOM    | 11,455.5                         | +5     | 2,877.3                    | +23    | 0.17               | 0.18            | +0.06 |
| 7   | 2.07               | 1.85            | -0.22 | AMERITECH              | 3,381.4                          | +7     | 512.5                      | +104   | 0.85               | 0.92            | +0.07 |
| 13  | 1.33               | 1.37            | +0.04 | GTE                    | 5,121.0                          | +3     | 695.0                      | +6     | 0.68               | 0.71            | +0.03 |
| 5   | 1.03               | 0.85            | -0.18 | PACIFIC TELESIS GROUP  | 2,275.0                          | -2     | 275.0                      | -12    | 0.61               | 0.64            | +0.03 |
| 1   | 0.98               | 1.12            | +0.14 | PANHANDLE EASTERN      | 1,133.7                          | +1     | 73.6                       | +44    | 0.44               | 0.49            | +0.05 |
| 5   | 2.93               | 3.01            | +0.08 | PP&L RESOURCES         | 682.2                            | +3     | 94.1                       | +22    | 0.50               | 0.55            | +0.05 |
| 9   | 1.56               | 1.72            | +0.16 | SBC COMMUNICATIONS     | 3,242.0                          | +8     | 534.3                      | +11    | 0.87               | 0.88            | +0.01 |
| 5   | 0.66               | 0.67            | +0.01 | SPRINT                 | 3,442.3                          | +6     | 268.5                      | +17    | 0.71               | 0.76            | +0.05 |
| 3   | 0.63               | 0.52            | -0.11 | UNICOM                 | 2,190.9                          | +18    | 424.3                      | +51    | 1.48               | 1.90            | +0.42 |
| 7   | 1.40               | 1.40            | —     |                        |                                  |        |                            |        |                    |                 |       |
| 9   | 1.57               | 1.74            | +0.17 |                        |                                  |        |                            |        |                    |                 |       |
| 2   | 1.58               | 1.62            | +0.04 |                        |                                  |        |                            |        |                    |                 |       |

† First-quarter results

†† Fourth-quarter results

NM = not meaningful

NA = not available

\*EPS adjusted for special items

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES. EARNINGS ESTIMATE DATA PROVIDED BY I/B/E/S INTERNATIONAL INC.

† First-quarter results

†† Fourth-quarter results

NM = not meaningful

NA = not available

\*EPS adjusted for special items

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES. EARNINGS ESTIMATE DATA PROVIDED BY I/B/E/S INTERNATIONAL INC. NEW YORK, NY. I/B/E/S IS A REGISTERED TRADEMARK OF I/B/E/S INTERNATIONAL INC.

Sherlund estimates that there are 1 million copies of Win95 sitting on the shelves—roughly two quarters' worth. And retailers confirm that sales are slowing, though some say they are dropping off a cliff. "The first few weeks, we couldn't keep it on store shelves, but it has tapered off," says Josh Marmorek, a Microsoft employee at Fry's Electronics store in Silly. Microsoft says its worries are much less than what you hear. Execu-



tives concede that Win95 sales have slowed from the initial frenzy, when 1 million copies were sold in the first four days. They also acknowledge that there is plenty of stock on store shelves, and if retailers are unhappy with that, Microsoft will have to take some of it back. But Microsoft doesn't think that's likely: The company is expecting Win95 to sell well during the typically heady Christmas quarter. Says Brad Chase, Microsoft's general manager of the Personal Systems division: "Sales

have dropped materially from the first week's numbers. But it's sort of like hitting four grand slams in a game to hitting one grand slam. Sales are still incredibly high."

One factor in Microsoft's favor: Win95 sales are shifting from consumers' buying upgrade packages to consumers' buying PCs with Win95 preinstalled. Of the 7 million Win95 copies sold, 4 million went to PC makers. And that is expected to climb in the fourth quarter, when analysts predict PC sales will grow a mighty 30%. If that's the case, the buzz may be the next thing that tapers off.

By Kathy Rebello in San Francisco, with Amy Cortese in New York





JAPAN

## WHY JAPAN'S BANKS HAVE A FRIEND IN WASHINGTON

The Fed wants to avert a panic—and a sell-off of U.S. Treasuries

To global financial experts, the stunning disclosure at an Oct. 16 hearing on Capitol Hill only fed their worst fears about the depth of Japan's banking woes. House Banking Committee Chairman James A. Leach (R-Iowa) revealed that the Federal Reserve had privately promised Japanese officials that the U.S. stood ready to provide emergency liquidity to avert a financial crisis. "This is further confirmation that they have world-class problems with their banking system," says Bert Ely, an Alexandria (Va.) banking-industry consultant.

But the Fed wasn't simply promising altruistically to help a longtime ally in trouble. The U.S. has a great stake in Japan's shaky banking system: Problems there could quickly spread to the U.S., driving up interest rates, depressing real estate, and sending the dollar on another downward spiral. These negative consequences could result from a sell-off of U.S. assets by the Japanese government to rescue its banks.

**SCARY SPECTER.** The failure of just three small Japanese lenders already has virtually depleted Tokyo's \$10 billion deposit-insurance fund. And with public sentiment running against a taxpayer-financed bailout, financial experts worry that Japan's government may have to

dip into its vast \$180 billion reserve of foreign holdings—nearly all in U.S. Treasuries—to cover future bank losses. Private Japanese investors, who hold at least \$40 billion more in U.S. Treasuries, also might start selling.

That's why the Fed swung into action. The central bank isn't talking, but Leach staffers say the Fed is offering repurchase agreements: The Japanese government could borrow cash from the Federal Reserve Bank of New York using its Treasury holdings on deposit at the bank as collateral. This would provide the cash Tokyo might need to cover losses at U.S. affiliates of Japanese banks—which control \$66 billion.

Leach says Tokyo isn't likely to need cash any time soon. But bond traders fear that the mere specter of a Japanese sell-off would trigger a surge in interest rates and help stall a less-than-robust expansion in the U.S. And many traders already are jittery, fearing that a budget stalemate in Washington could cause the government

**STREET TALK**  
Did Greenspan beg off public testimony about a Fed loan offer for fear of spooking the markets?

to default on bonds. Testimony mounted on Oct. 17 when Treasury Secretary Robert E. Rubin vowed to scale back any coming Treasury auction unless Congress raises the federal ceiling.

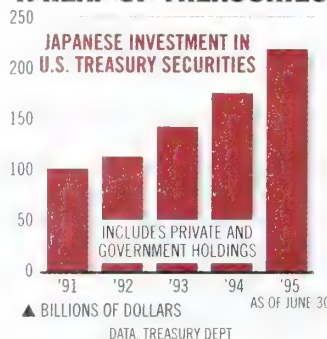
If no compromise is reached,

U.S. default could reverse the powerful bond rally fueled by Japan's recent aggressive purchase of Treasuries to ease the surging yen. And a Japanese sell-off of U.S. Treasuries would only make matters worse. During the first half of 1995, Japanese buyers sopped up \$10 billion worth of U.S. notes and bills, just one-third more than they did in the same period in 1994 (chart). "Japan has been serving the 13th Federal Reserve District," says William P. Sterling, an economist and investment strategist for New York-based BEA Associates.

**STEAM VALVE.** The Fed plan is designed to ease the pressure on Japanese banks. They generally are more dependent on short-term global money markets than their U.S. counterparts on funding from short-term global money markets, which could shut out Japan at a high price. Indeed, Japanese banks already are paying higher premiums—0.25 percentage points more than U.S. and European banks pay for dollar borrowing in London. That's pushing the cost of borrowing above the return on U.S. commercial loans and could force Japanese banks to trim their portfolios. With Japan accounting for 17% of U.S. corporate lending and 20% of syndicated business commitments, Japanese pullout could drive up commercial rates for U.S. corporate borrowers. It also could leave domestic banks hard-pressed to fill the void. "If you think Chemical [Bank] is going to absorb the 20%?" asks one banker.

To be sure, Leach notes, Fed Chairman Alan Greenspan has assured him that "does not expect an unmanageable situation to arise." Yet Japan's financial situation is sensitive enough for Greenspan to beg for a request by Leach to testify about it in public, perhaps for fear of spooking the market.

### A HEAP OF TREASURIES





vately, U.S. officials appeared concerned last July when the Nikkei market index drifted close to—the critical level that could decapitate Japanese banks' capital reserves, consist largely of stock holdings. prompted the U.S. and Japan to a massive dollar-buying spree, g the yen down 25% since April. result: The Nikkei rose to 18,000,

and the value of equity holdings by Japanese banks soared from \$30 billion to \$130 billion, giving Tokyo breathing room to implement financial reforms.

These days, U.S. officials are more optimistic about the longer-term prospects for Japanese banks, though they're hardly bullish. "The Japanese banks are somewhere between the U.S. system of the 1930s and U.S. system of the

1990s—but probably closer to the 1990s," says one senior U.S. official. Reassuring words. But his oblique allusion to the bank crisis that ushered in the Depression shows just how seriously the U.S. government is taking the fragility of Japan's banks.

*By Dean Foust, with Amy Barrett, in Washington and Kelley Holland in New York*

## COMMENTARY

By Howard Gleckman

# ONE ROOF FOR ALL ECONOMIC DATA

buried deep in their massive 1996 budget, House Republicans have come up with a horrible idea—littering Commerce Dept. statistics-gathering agencies throughout government. The Bureau of Economic Analysis, which produces such vital data as the gross domestic product, would be shipped off to the Labor Dept. to be merged with its longtime bureaucratic rival, the Bureau of Labor Statistics. The Census Bureau would head to the Office of Management & Budget for next year only. Then, it would move once again, to an agency to be named later.

All this is part of the House GOP's effort to dismantle the Commerce Dept. "The American people will literally see a velvet chair taken out of the White House and put in a museum," says House Majority Leader Richard K. Armey (R-Texas). But sending number-crunchers wandering

the bureaucratic wilderness won't save government costs. And it is the wrong solution to a serious problem: In a rapidly changing economy, reliable economic data are becoming increasingly important, even as shrinking resources make it tougher to gather accurate information. "Splitting up [statistics agencies] up makes no sense whatsoever," says Maurice H. Haver, president of the New York economic consulting firm Haver Associates. "It only makes a very fragmented system worse."

**POWERFUL INTERESTS.** The real solution is to merge all the far-flung statistical agencies into a single office—much like America's northern neighbor has done with Statistics

Canada. That might not save much money, either. But it would improve data collection and analysis in three important ways.

First, in an era of fiscal austerity, a single agency reporting directly to its own congressional oversight committee would have more visibility—and the clout to fight for the funding it would need to do its job. Today,

impact of new technologies. It would also make it politically easier to shift resources to meet congressional mandates, such as satisfying the current demand to improve the Consumer Price Index.

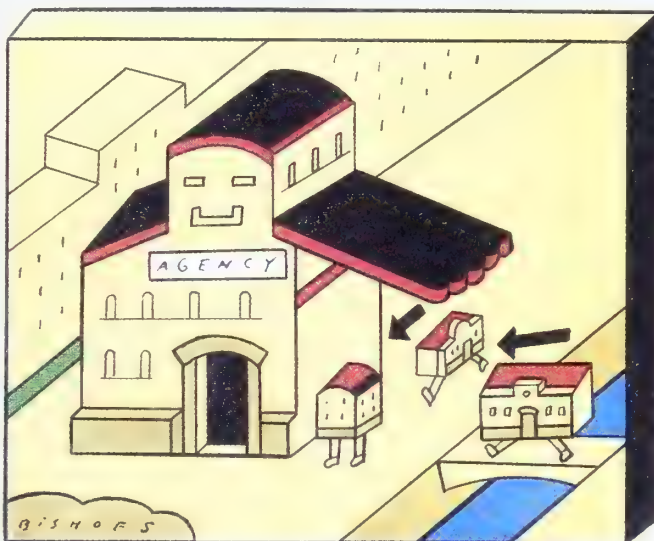
Finally, a single operation would encourage sharing of information, which is something that U.S. law bars some government agencies from doing now, typically citing privacy and secrecy concerns. The Census Bureau, for example, is prohibited from providing finely detailed "microdata" to other offices.

According to a recent survey, nearly 60% of private economists back a merger of government statistics offices. Unfortunately, the Clinton Administration is divided on the idea of creating a single agency. Top Commerce officials support the plan. "A single statistical agency deserves consideration," says Everett M. Ehrlich, Commerce

Under Secretary for economic affairs. But the Labor Dept., which fears losing its own data-gathering operations, opposes any merger. Concedes a top White House official: "As long as they are opposed, nothing is going to happen on this."

The upshot: The green-eyeshade types face shrinking budgets and more balkanization in the GOP's enthusiasm to bag itself a department. Republicans defend their actions by saying they might eventually back a single statistics agency. Great—but why wait? Get on with it today, or leave matters alone.

*Gleckman covers economic policy from Washington.*



the statistical offices are tiny pieces of massive departments, essentially defenseless in the face of voracious budget-cutters. Even before its proposed spin-off, for instance, BEA faces a 25% budget cut.

Just as important, a single agency can allocate resources more efficiently. The sad fact is, the nation has far more data on the production of cow chips than on computer chips. The reason: Powerful farm interests insist on protecting the Agriculture Dept.'s massive statistical programs. A consolidation would give a new agency the flexibility to refocus efforts on critical issues facing the U.S. in a new global economy, such as how to quantify productivity gains or the



PEOPLE

# WHO'S THAT GUY IN CHRYSLER'S FRONT SEAT?

Car dealer Louis Patane is suddenly a top marketing exec

Last summer, when Chrysler President Robert A. Lutz wanted to get a showroom-level perspective on the auto market, he called up one of his favorite car dealers, Louis P. Patane. For half an hour, Patane—owner of two small Chrysler dealerships in Avondale, Ariz.—chatted with Lutz about marketing strategy, customer relations, and Chrysler's model lineup. Lutz liked what he heard and offhandedly suggested that Patane come to work for him. A week later, Patane surprised Lutz by deciding to sell his lucrative dealerships and take the offer.

Patane's sudden ascent from owner of a suburban car dealership to a spot near the top of Chrysler Corp.'s marketing hierarchy is causing a stir in Motown. In September, Patane took the newly created position of executive director of brand marketing, and some insiders expect him to be named a vice-president soon. Fellow car dealers wonder just how the obscure, 45-year-old Patane managed to leapfrog into Chrysler's management ranks. "This guy only sold 30 cars a month. What does he know?" snipes Martin J. "Hoot" McInerney, a Detroit-area megadealer.

**"RUFFLED FEATHERS."** Lutz argues that Chrysler needs the fresh eye of an outsider to help get its marketing shaped up. Last fall, General Motors Corp. ventured far outside the car industry when it hired former Bausch & Lomb President Ronald L. Zarrella as its top marketing executive. Like GM, Chrysler must fashion distinct identities for its blurry brands, and a dealer's perspective may help, Lutz figures. "Marketing strategies that look

good at the Pentagon level might not look too good in the field," he says.

A corporate heavyweight like Zarrella is one thing. But Patane's arrival at Chrysler's Highland Park (Mich.) headquarters has "ruffled some feathers" among the company's marketing honchos, says one insider. The current team believes it already has a good plan for solving the company's mar-



## LOUIS PATANE

**BORN** Jan. 23, 1950

**EDUCATION** Diploma in computer programming, Rochester (N.Y.) Business Institute

**CAREER** Started his automotive career in 1979 managing a machining company specializing in race-car engines.

Bought Louis Dodge in Avondale, Ariz., in 1986 and added a Chrysler-Plymouth dealership eight years later. His challenge: Fixing Chrysler's brand problems with Eagle and Plymouth.

**REPUTATION** A "car guy" who races dragsters in his off hours and gets on with engineers.

keting problems by repositioning its brands: Plymouth is to stand for value, Chrysler for prestige, and Eagle is to be given a sporty image that will appeal to import buyers. Results, however, haven't been stunning: Chrysler-Plymouth sales slid 15% through September compared

with the first nine months of 1994; the Eagle, rumored to be headed for extinction, still has less than a 1% share of the U.S. market, despite a \$100-million advertising blitz.

What does Patane bring to the table? The soft-spoken ex-dealer isn't giving details for now. But associates say that as a member of the National Independent Dealer Council he did a good job of scrutinizing Chrysler's brands and finding a brand-savvy approach to local advertising. He persuaded Phoenix Dodge dealers, for example, to produce a sophisticated TV spot extolling the virtues of the Ram pickup truck without blaring price pitch.

**DELICATE BALANCE.** Like Lutz, Patane is a car guy. He earned a computer programming diploma in Rochester, N.Y., while working in auto-body and machine shops. He owned a car wash and a gas station before buying a Dodge dealership in 1986. "I came into this business through the back end, which gives me a strong customer viewpoint," Patane says through a spokesman. On weekends, he races dragsters on the National Rod Assn. circuit.

That's hardly a high-powered résumé, though. And at best Patane faces a delicate balancing act at Chrysler. He must feed dealers' appetite for creative promotions and advertising while tinkering with brand identities at the corporate level. A major fix of Chrysler's marketing muddle—dropping the Eagle name



**BRAND BOMB:** The Eagle hasn't floated

repositioning Plymouth—will risk confusing consumers if it isn't done well.

Still, with Patane's appointment, Chrysler is sending a message to Chrysler's marketing team: Get focused on the customer trolling showroom floors.

By Bill Vlasic in Detroit

"Marketing strategies that look good at the Pentagon level," says Chrysler's Lutz, might not work in the field



# AMERICAN STOCK EXCHANGE COMPOSITE TRANSACTIONS

| A-B-C |     |     |     |     |     |     |     |     |     | D-E-F |     |     |     |     |     |     |     |     |     | G-H-I |     |     |     |     |     |     |     |     |     | J-K-L |     |     |     |     |     |     |     |     |     | M-N-O |     |     |     |     |     |     |     |     |     | P-Q-R |     |     |     |     |     |     |     |     |     | S-T-U |     |     |     |     |     |     |     |     |     | V-W-X-Y-Z |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |     |      |
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| 100   | 101 | 102 | 103 | 104 | 105 | 106 | 107 | 108 | 109 | 110   | 111 | 112 | 113 | 114 | 115 | 116 | 117 | 118 | 119 | 120   | 121 | 122 | 123 | 124 | 125 | 126 | 127 | 128 | 129 | 130   | 131 | 132 | 133 | 134 | 135 | 136 | 137 | 138 | 139 | 140   | 141 | 142 | 143 | 144 | 145 | 146 | 147 | 148 | 149 | 150   | 151 | 152 | 153 | 154 | 155 | 156 | 157 | 158 | 159 | 160   | 161 | 162 | 163 | 164 | 165 | 166 | 167 | 168 | 169 | 170       | 171 | 172 | 173 | 174 | 175 | 176 | 177 | 178 | 179 | 180 | 181 | 182 | 183 | 184 | 185 | 186 | 187 | 188 | 189 | 190 | 191 | 192 | 193 | 194 | 195 | 196 | 197 | 198 | 199 | 200  |
| 200   | 201 | 202 | 203 | 204 | 205 | 206 | 207 | 208 | 209 | 210   | 211 | 212 | 213 | 214 | 215 | 216 | 217 | 218 | 219 | 220   | 221 | 222 | 223 | 224 | 225 | 226 | 227 | 228 | 229 | 230   | 231 | 232 | 233 | 234 | 235 | 236 | 237 | 238 | 239 | 240   | 241 | 242 | 243 | 244 | 245 | 246 | 247 | 248 | 249 | 250   | 251 | 252 | 253 | 254 | 255 | 256 | 257 | 258 | 259 | 260   | 261 | 262 | 263 | 264 | 265 | 266 | 267 | 268 | 269 | 270       | 271 | 272 | 273 | 274 | 275 | 276 | 277 | 278 | 279 | 280 | 281 | 282 | 283 | 284 | 285 | 286 | 287 | 288 | 289 | 290 | 291 | 292 | 293 | 294 | 295 | 296 | 297 | 298 | 299 | 300  |
| 300   | 301 | 302 | 303 | 304 | 305 | 306 | 307 | 308 | 309 | 310   | 311 | 312 | 313 | 314 | 315 | 316 | 317 | 318 | 319 | 320   | 321 | 322 | 323 | 324 | 325 | 326 | 327 | 328 | 329 | 330   | 331 | 332 | 333 | 334 | 335 | 336 | 337 | 338 | 339 | 340   | 341 | 342 | 343 | 344 | 345 | 346 | 347 | 348 | 349 | 350   | 351 | 352 | 353 | 354 | 355 | 356 | 357 | 358 | 359 | 360   | 361 | 362 | 363 | 364 | 365 | 366 | 367 | 368 | 369 | 370       | 371 | 372 | 373 | 374 | 375 | 376 | 377 | 378 | 379 | 380 | 381 | 382 | 383 | 384 | 385 | 386 | 387 | 388 | 389 | 390 | 391 | 392 | 393 | 394 | 395 | 396 | 397 | 398 | 399 | 400  |
| 400   | 401 | 402 | 403 | 404 | 405 | 406 | 407 | 408 | 409 | 410   | 411 | 412 | 413 | 414 | 415 | 416 | 417 | 418 | 419 | 420   | 421 | 422 | 423 | 424 | 425 | 426 | 427 | 428 | 429 | 430   | 431 | 432 | 433 | 434 | 435 | 436 | 437 | 438 | 439 | 440   | 441 | 442 | 443 | 444 | 445 | 446 | 447 | 448 | 449 | 450   | 451 | 452 | 453 | 454 | 455 | 456 | 457 | 458 | 459 | 460   | 461 | 462 | 463 | 464 | 465 | 466 | 467 | 468 | 469 | 470       | 471 | 472 | 473 | 474 | 475 | 476 | 477 | 478 | 479 | 480 | 481 | 482 | 483 | 484 | 485 | 486 | 487 | 488 | 489 | 490 | 491 | 492 | 493 | 494 | 495 | 496 | 497 | 498 | 499 | 500  |
| 500   | 501 | 502 | 503 | 504 | 505 | 506 | 507 | 508 | 509 | 510   | 511 | 512 | 513 | 514 | 515 | 516 | 517 | 518 | 519 | 520   | 521 | 522 | 523 | 524 | 525 | 526 | 527 | 528 | 529 | 530   | 531 | 532 | 533 | 534 | 535 | 536 | 537 | 538 | 539 | 540   | 541 | 542 | 543 | 544 | 545 | 546 | 547 | 548 | 549 | 550   | 551 | 552 | 553 | 554 | 555 | 556 | 557 | 558 | 559 | 560   | 561 | 562 | 563 | 564 | 565 | 566 | 567 | 568 | 569 | 570       | 571 | 572 | 573 | 574 | 575 | 576 | 577 | 578 | 579 | 580 | 581 | 582 | 583 | 584 | 585 | 586 | 587 | 588 | 589 | 590 | 591 | 592 | 593 | 594 | 595 | 596 | 597 | 598 | 599 | 600  |
| 600   | 601 | 602 | 603 | 604 | 605 | 606 | 607 | 608 | 609 | 610   | 611 | 612 | 613 | 614 | 615 | 616 | 617 | 618 | 619 | 620   | 621 | 622 | 623 | 624 | 625 | 626 | 627 | 628 | 629 | 630   | 631 | 632 | 633 | 634 | 635 | 636 | 637 | 638 | 639 | 640   | 641 | 642 | 643 | 644 | 645 | 646 | 647 | 648 | 649 | 650   | 651 | 652 | 653 | 654 | 655 | 656 | 657 | 658 | 659 | 660   | 661 | 662 | 663 | 664 | 665 | 666 | 667 | 668 | 669 | 670       | 671 | 672 | 673 | 674 | 675 | 676 | 677 | 678 | 679 | 680 | 681 | 682 | 683 | 684 | 685 | 686 | 687 | 688 | 689 | 690 | 691 | 692 | 693 | 694 | 695 | 696 | 697 | 698 | 699 | 700  |
| 700   | 701 | 702 | 703 | 704 | 705 | 706 | 707 | 708 | 709 | 710   | 711 | 712 | 713 | 714 | 715 | 716 | 717 | 718 | 719 | 720   | 721 | 722 | 723 | 724 | 725 | 726 | 727 | 728 | 729 | 730   | 731 | 732 | 733 | 734 | 735 | 736 | 737 | 738 | 739 | 740   | 741 | 742 | 743 | 744 | 745 | 746 | 747 | 748 | 749 | 750   | 751 | 752 | 753 | 754 | 755 | 756 | 757 | 758 | 759 | 760   | 761 | 762 | 763 | 764 | 765 | 766 | 767 | 768 | 769 | 770       | 771 | 772 | 773 | 774 | 775 | 776 | 777 | 778 | 779 | 780 | 781 | 782 | 783 | 784 | 785 | 786 | 787 | 788 | 789 | 790 | 791 | 792 | 793 | 794 | 795 | 796 | 797 | 798 | 799 | 800  |
| 800   | 801 | 802 | 803 | 804 | 805 | 806 | 807 | 808 | 809 | 810   | 811 | 812 | 813 | 814 | 815 | 816 | 817 | 818 | 819 | 820   | 821 | 822 | 823 | 824 | 825 | 826 | 827 | 828 | 829 | 830   | 831 | 832 | 833 | 834 | 835 | 836 | 837 | 838 | 839 | 840   | 841 | 842 | 843 | 844 | 845 | 846 | 847 | 848 | 849 | 850   | 851 | 852 | 853 | 854 | 855 | 856 | 857 | 858 | 859 | 860   | 861 | 862 | 863 | 864 | 865 | 866 | 867 | 868 | 869 | 870       | 871 | 872 | 873 | 874 | 875 | 876 | 877 | 878 | 879 | 880 | 881 | 882 | 883 | 884 | 885 | 886 | 887 | 888 | 889 | 890 | 891 | 892 | 893 | 894 | 895 | 896 | 897 | 898 | 899 | 900  |
| 900   | 901 | 902 | 903 | 904 | 905 | 906 | 907 | 908 | 909 | 910   | 911 | 912 | 913 | 914 | 915 | 916 | 917 | 918 | 919 | 920   | 921 | 922 | 923 | 924 | 925 | 926 | 927 | 928 | 929 | 930   | 931 | 932 | 933 | 934 | 935 | 936 | 937 | 938 | 939 | 940   | 941 | 942 | 943 | 944 | 945 | 946 | 947 | 948 | 949 | 950   | 951 | 952 | 953 | 954 | 955 | 956 | 957 | 958 | 959 | 960   | 961 | 962 | 963 | 964 | 965 | 966 | 967 | 968 | 969 | 970       | 971 | 972 | 973 | 974 | 975 | 976 | 977 | 978 | 979 | 980 | 981 | 982 | 983 | 984 | 985 | 986 | 987 | 988 | 989 | 990 | 991 | 992 | 993 | 994 | 995 | 996 | 997 | 998 | 999 | 1000 |

"We sell the most valuable commodity. Time. Our core business is selling tv, radio and cable airtime. We're creating new businesses at home and expanding abroad," says Tom Olson, President and CEO of Katz Media Group Inc., an AMEX IPO in April 1995. "Since listing, the AMEX has worked with us every day. They initiate our participation in AMEX industry conferences, analyst seminars and institutional meetings to give us visibility. That's the commodity a \$290 million company needs." **TOM OLSON IS BIG ON THE AMEX.**



## MEDICINE

# THE \$665 MILLION MARKET NOBODY TALKS ABOUT

There's a burst of new treatments for impotence

**P**rostate surgery probably saved Wallace L. Kouwenhoven's life seven years ago. But the operation to remove his cancerous prostate came at a cost: The former computer-systems chief for Philips Electronics North America soon found himself suffering from what now is called erectile dysfunction. Barely 60 years old, he was impotent.

Luckily, Kouwenhoven's doctors had a solution. They put the Long Island man on Caverject, a then-experimental drug that can restore potency. Recently approved by regulators, put onto the market by Upjohn Co. in late August, and backed by a national ad campaign launched Oct. 17, the drug is the newest attack on a problem plaguing perhaps 20 million U.S. men. "The results are astounding," says Kouwenhoven, who has injected himself with the medicine up to four times monthly for more than six years.

**PELLETS AND PILLS.** Thanks to such treatments, impotence is no longer a seemingly irreversible byproduct of aging. Drug therapy is coming into its own, alongside such time-tested devices as inflatable implants, bendable rods, and vacuum pumps. And more approaches are in the works that will likely boost what analysts figure is already better than a \$665 million-a-year market: By early next year, Vivus Inc. in Menlo Park, Calif., expects to seek regulatory approval for a tiny, insertable pellet for men who shy away from Caverject's needle. Drug giant Pfizer Inc. may be less than three years away from commercializing an anti-impotence pill. "In the 1990s, there is no reason for any man not to get erections," says Dr. Kenneth A. Goldberg, a Dallas urologist.

Maybe so, but restoring the old *joie de vivre* is getting more expensive. Caverject goes for \$20 to \$25 a shot. For many men, that will compare unfavorably with the homemade mixtures of the drug and one or two others

that urologists for years have sold privately for as little as \$3 a dose. Vivus says its pellet will be priced about the same as Caverject. "Prices are going up," complains Dr. Brett C. Mellinger, chairman of urology at Winthrop University Hospital in Mineola, N.Y. He frets that some of the new approaches may not catch on because of cost.

Still, Caverject may help bring many more sufferers forward to get help. Upjohn's new national print advertising campaign will be aimed at impotence, and the company will soon begin testing radio ads. The ads provide an 800 number from which callers will be referred to local impotence specialists. The company hopes the pitch will be as successful as the ones for Rogaine, its baldness treatment.

For many men, though, Caverject may prove a tough sell. Urologists say their patients often feel uneasy about giving themselves an injection, even just a tiny one, each time they feel amorous. Says Dr. Fran E. Kaiser, a professor of medicine at St. Louis University who has worked on clinical studies for various treatments: "Some men can't get over the psychic block of us putting a needle into their favorite body part." Indeed, the drug has a 40%

drop-out rate, even though it works well for 80% of the men who use it.

There are alternatives, of course. Some doctors expect renewed interest in vacuum devices, such as the \$400 ErecAid reusable pump. Others are gearing up for an increase in \$15,000 prosthetic implant operations, despite a smattering of lawsuits brought by lawyers who



**TOUGH SELL:** Kaiser says some can't deal with shots

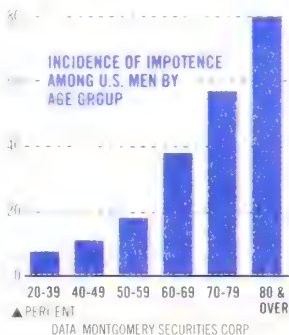
argue the silicone in them may be hazardous. Pfizer, while it works on its denafil pill, is remaining in the impotence business, along with a smaller California-based Mentor Corp. "These treatments are bringing people out of the closet," says Mentor's urology product manager, Craig Fortier.

**SUFFERING IN SILENCE.** As baby boomers age, the problem seems sure to become even more common. Diseases such as diabetes can cause impotence, and medications for common conditions such as high blood pressure. Simple and can be a cause, though experts don't think most erectile problems are physical rather than psychological. More than 10 million of men with the problem suffer quietly, with only a fraction—perhaps just a few hundred thousand annually—seeking treatment, according to Montgomery Securities Corp. analyst Leonard S. Yaffe.

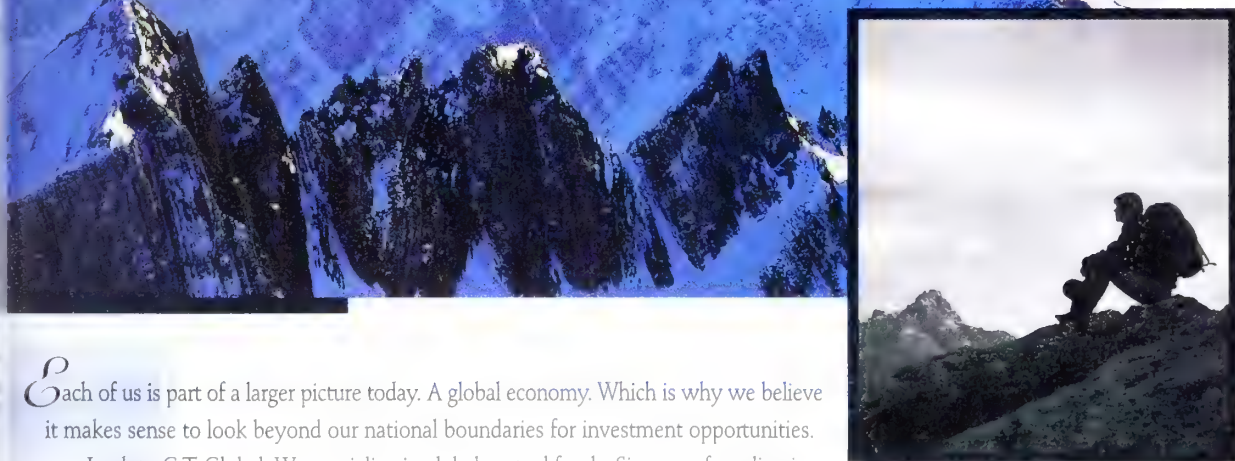
The new tools are hardly perfect. Implants, for instance, can fail or even lead to infections. And injections and vacuum pumps hardly make for spontaneity. For many men, they're far better than the alternative. With the new approaches, says Dr. Arnold Melman, chairman of urology at the Albert Einstein College of Medicine-Montefiore Medical Center in New York City, "you really can make a lot of people very happy."

By Joseph Weber in Philadelphia

## AN AGE-OLD PROBLEM



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## RETAILING

## CAN TJX TURN OFF-PRICE ON?

Even this smart shopper's strategy may not be enough



CEO CAMMARATA: "It's a fallacy to think off-price is dead"

**B**ernard Cammarata, CEO of off-price retailing giant TJX Cos., has spent a career hunting bargains. On Oct. 16, he found a deal he couldn't pass up: For \$550 million, he will buy Marshalls Inc., a 495-store chain that had been dogging his backside for years. In one fell swoop, Cammarata took out his largest competitor, nearly doubled TJX's \$3.8 billion in annual sales, and sent shivers throughout his now much smaller rivals. "This is the best buy I've ever made," he boasts.

But in today's sepulchral retail climate, Cammarata may only be getting what he pays for. Nearly all off-price chains—which specialize in discounted name-brand clothing—are reeling from a prolonged slump in apparel sales and heightened competition from department stores. Discount chains are facing similar problems: On Oct. 16, Kmart Corp., the nation's second-largest retailer, publicly refuted suggestions that it file for Chapter 11. Two days later, Jamesway Corp. said it would go out of business.

Can off-price regain viability? TJX recorded year-over-year declines in same-store sales in 14 of the past 21 months, and "there's no turnaround in sight," for the apparel business, says Lawrence H. Wortzel, a Boston University marketing professor. Retorts Cammarata: "It's a fallacy to think off-price is dead." Investors aren't so sure. Although TJX shares have jumped more than 25%, to \$15, since rumors of the deal leaked early in October, they aren't worth much more than in 1988. Sales have soared to \$4.2 billion in that time, from \$1.6 billion.

The bulls buying up TJX's shares are

betting that if anyone can revive off-price retailing, it's Cammarata. He skipped college to start his retailing career at 17, as a \$50-a-week stockroom clerk at Macy's. Then came stints as a buyer for J.W. Mays in Brooklyn, Wilmington Dry Goods, and Marshalls. In 1976, the owners of the former Zayre Corp. recruited him to start a chain of off-price stores, T.J. Maxx Stores.

Cammarata, 55, has been a dominant force in off-price retailing ever since. Prior to buying Marshalls, TJX owned 571 T.J. Maxx stores and had lifted sales at or near double-digit annual rates for most of the past 20 years. Cammarata "is highly focused, and he knows the industry better than anyone else," says a rival.

But as department stores have cut costs, TJX's net profit margins have narrowed to 2%, from 3.5% in 1993. Cammarata intends to boost margins again by closing 190 Marshalls and T.J. Maxx stores, pruning \$70 million in expenses over three years. He'll use the combined company's increased buying power to extract lower prices from vendors.

The bad news: Cammarata expects apparel sales to stay flat. "Profitable market share gains in apparel are difficult," he says. T.J. Maxx stores may show moderate sales gains, but sales at Marshalls are likely to decline through the consolidation, he says. For now, TJX's top-line growth will have to come from overseas, and from a U.S. chain called HomeGoods. Cammarata's biggest deal may help ease the pain—but it likely won't solve the problem.

By Geoffrey Smith in Boston

## DEALS

## WATCH WARREN WIN WITH WELLS

A boon for Buffett in Wells Fargo's run at First Interstate

**W**arren E. Buffett wins again. On Oct. 18, just a bit more than 18 months after the investor logged a big gain from Disney's deal to purchase Cap Cities/ABC, another right Buffett holding, San Francisco-based Wells Fargo & Co., made an untimed bid for Los Angeles-based First Interstate Bancorp. The deal, valued at more than \$10 billion, would be among the largest in U.S. banking history and the industry's first major hostile purchase since Bank of New York Co.'s bid for Irving Bank Corp. in 1987. "It's a brilliant move," says Lloyd Greif, owner of Los Angeles' Greif & Co. and an investor in both banks.

Wall Street couldn't have agreed more. Both stocks shot up on the news. First Interstate climbed 32%, to 160, and Wells Fargo closed at 229, up 34% on a \$98 million gain for Buffett's 13.3% stake in the company. Wells Fargo called the market's move a clear vote of support for its offer of approximately \$14 1/2 for each First Interstate share.

**"DEEPLY DISAPPOINTED."** The two banks have talked in the past—as recently as the night before the announcement, according to Wells Fargo CEO Paul Horvath. He said he decided to step up the stake as a way of accelerating the merger. First Interstate, though, had not welcomed the move: "I am deeply disappointed that Wells Fargo would take this uninvited action," Chairman William Siart said in a statement. Siart said the bank's board is considering its options.

Analysts see the deal as too costly, likely not to get done. "You get in-mid-cost savings and Wells management is likely able to apply itself to a much bigger and more geographically diverse franchise," says Thomas K. Brown, a bank analyst at Donaldson, Lufkin & Jenrette.

Anyway, there are few other bidders likely to match Wells Fargo's offer. Reluctant though it may be, First Interstate will likely find itself the latest casualty in a binge of banking buyouts. Buffett, meanwhile, will be able to add Wells Fargo's conquest as another victory for his books.

By Nanette Byrnes in Los Angeles and Kelley Holland in New York



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HOLLYWOOD

# OUT OF THE INKLESS WELL

In *Toy Story*, Disney's characters were "drawn" by computer

They may be mere cartoons to the rest of the world. But to Walt Disney Co., its animated films are money machines, producing billions in revenues in recent years. With the rush of new cash, however, the salaries of animators have soared. Little wonder, then, that Disney executives seem pleased by *Toy Story*, which they are trumpeting as Hollywood's first computer-animated movie.

The economics of *Toy Story*, which will hit movie theaters on Nov. 12, are compelling. Produced at rows of Silicon Graphics Inc. workstations at Steven P. Jobs's Pixar animation studio outside San Francisco, the 3-D-like film that brings to life toys in a little boy's room was made with just 27 animators vs. the 70 or so who inked *Pocahontas*. With animators making \$100,000-plus a year, that amounts to savings of more than \$10 million, which helped Disney hold the film's budget to an estimated \$30 million.

**ACE CARD.** The question now is whether *Toy Story* will do better than 1993's *The Nightmare Before Christmas*, Disney's lackluster first attempt at making an animated film without pencils and paint. Like Disney, Apple Computer founder Jobs, who bought Pixar from filmmaker George Lucas in 1985 for \$10 million, has a lot riding on the answer: He filed an initial stock offering on Oct. 10 to sell 16% of Pixar for up to \$82 million.

*Toy Story* has a big plus going for it: It's one of the few children's movies among this year's holiday offerings (table).

The other hotly anticipated films are Warner Brothers Inc.'s *Ace Ventura 2*, with rubber-faced Jim Carrey, and Sony Corp.'s *The American President*, starring Michael Douglas as a date-happy divorced president.

Given the dearth of alternatives, kids and their parents may warm to *Toy Story*'s rounded computer images. It

features a pull-toy cowboy, whose voice is supplied by Tom Hanks, and Tim Allen giving voice to a plastic space ship called Buzz Lightyear. To appeal to adults, it also is laced with jokes aimed at adults. (A plastic dinosaur annoys him because he came from "an LBO that was bought by Mattel.")

Still, this film has some shortcomings. *The Lion King* and other recent Disney hits were packed with Broadway-quality songs; *Toy Story* has three forgettable numbers by singer-songwriter Randy Newman. It's also loaded with well-known toys such as Playskool's Potato Head and Ohio Art Co.'s Elinor Sketch, so only two *Toy Story* characters have been licensed.

Disney already is gearing up its



**ANIMATED DISCUSSION:** Virtual Allen and Hanks

midable marketing machine to create a buzz around the new toy. Among the strategies: *Toy Story* parade at the Disney World in Orlando, Fla., a Disney Channel special, and advertisements for *Toy Story* leading off the 7 min. *Cinderella* video cassette it has shipped. There will be plenty of cross-promotions, too. \$125 million worth, Disney says. Among the giveaways by Mr. Potato Head are orange juice,urger King, and Fritos. In L.A., Disney even has put \$1.3 million in new funhouse featuring rides and shows based on the movie.

More projects are in the works if *Toy Story* succeeds. Disney plans to release a pair of CD-ROM games and is contemplating an animated TV series based on the movie. At Pixar, which has agreed to produce two films for Disney, is working on a second film about insects called *A Bug's Life*. Quite a brouhaha over the pack of computer-generated toys.

By Ronald Groves  
Barbank, Calif.  
Kathy Rebello in San Francisco

## Tinseltown Noel

STUDIO

MARKET SHARE\*

**DISNEY** *Toy Story*, a \$30 million comedy, debuts on Nov. 22. Will America's kids warm to Don Rickles as Mr. Potato Head?

17.6%

**WARNER BROTHERS** *Ace Ventura 2: When Nature Calls* is due Nov. 10. This \$55 million comedy stars the bankable Jim Carrey.

15.5%

**UNIVERSAL** *Casino*, a \$58 million Martin Scorsese gangster flick with Robert DeNiro and Sharon Stone is set for Nov. 22. It's no *Godfather*, but should sell.

14.2%

**SONY** *Jumanji*, a \$70 million movie starring Robin Williams trying to escape from a board game. Sound confusing? So's the plot. Due Dec. 15.

12.3%

**PARAMOUNT** *Sabrina* features Harrison Ford and Julia Ormond in a \$36 million remake of Billy Wilder's 1954 romantic classic. Quality flick, but prospects are modest. Due Dec. 15.

11.3%

**FOX** *Waiting to Exhale*, a \$32 million black women's buddy film, is due Nov. 22. With this as its only release for the season, it won't be a Merry Christmas for Rupert Murdoch's crew.

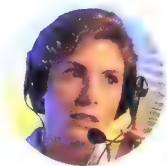
9.2%

DATA: VARIETY; EXHIBITOR RELATIONS CO.; COMPANY REPORTS

\* Share of box office receipts through Sept. 28



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EDITED BY KEITH H. HAMMONDS

## SCHACHT ANSWERS AT&T'S CALL

HENRY SCHACHT BECAME A Rust Belt legend by engineering one of the great industrial restructurings of the 1980s. As chief executive of Cummins Engine, he beat back Japanese rivals and cut costs 30%. Can he work his magic again? On Oct. 12, AT&T named Schacht, 60, chairman of its huge equipment spin-off. Schacht has just six to eight weeks in which to prepare the \$20 billion division for a public offering—in early 1996. At the same time, he must ready it to do battle without the advantage of AT&T's deep pockets. "It's a marvelous intellectual opportunity," he says. In the process, Schacht will

have to push into global markets, develop new technologies, and fight off competitors seeking to steal the business of the unit's most loyal customer—AT&T. Schacht vows to rely heavily on Bell Labs to keep the company on the cutting edge, despite industry rumors that the invention machine may be scaled back. "Bell Labs is the seed corn," he says. "We wouldn't do anything to harm it." A patient builder with an eye for the long haul—just what a \$20 billion startup needs.

## THE SENATE'S DULLER KNIFE

AS EXPECTED, THE SENATE Finance Committee wrapped up a \$245 billion tax-cut plan that proved little more than a scaled-down version of the House's \$350 billion package. The Senate bill cuts taxes on capital gains to 19.8% from 28% but does away with a new House-passed depreciation scheme and waters down alternative-minimum-tax relief. It adds a more generous expansion of individual retirement accounts and a deeper cut in estate taxes for owners of small businesses. The plan will be incorporated into the congressional budget measure—which President Clinton promises to veto. But he may well sign a further trimmed version as part of a compromise later on.

## PAIN AT NATIONAL MEDICAL CARE

LET IT NOT BE SAID THAT THE government is letting National Medical Care off easy. The kidney-dialysis and home-health-care company, slated to be spun off by W. R. Grace, revealed on Oct. 17 that it had received subpoenas demanding extensive documents for a federal

## HEADLINER: HARMONIA AXYRIDIS

### LADYBUG, LADYBUG

According to folklore, the ladybug is a harbinger of good luck. If so, the eastern U.S. is lousy with luck this fall. Call it the invasion of the *Harmonia axyridis*, an exotic Asian lady beetle seeking a winter home.

The insects' arrival has been a mixed blessing. As aphid-eaters, they're a boon to fruit and nut growers and organic gardeners. But to homeowners, they're pests, speckling walls and ceilings.

Most experts believe the *Harmonia* descended from stowaways on an Asian cargo ship that unloaded in New Orleans in 1988.

The skyrocketing population moved north through Alabama, Georgia, the Carolinas, and Virginia in 1990, then invaded the mid-Atlantic states.

"I think we're only seeing the tip of the iceberg," says Paul Schaefer, entomologist at the Agriculture Research Service in Newark, Del.

The result: a nuisance—apparently without natural predators that has nonetheless "nearly eliminated pecan aphids" in orchards they have colonized, says ARS entomologist Louis Tedders. Better than killing bees, anyway.

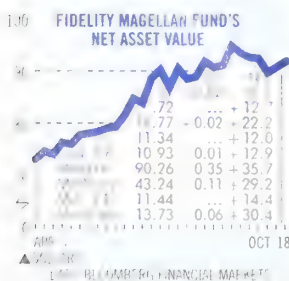
By Naomi Freundlich



## CLOSING BELL

### GAS GUZZLER

Even Fidelity Investments' Jeffrey Vinik doesn't always outsmart the stock market. His Magellan Fund is up 38% this year—but not because of his huge stake in General Motors. In January, GM showed up as one of Magellan's top 10 holdings; by June 30, Fidelity's combined holdings accounted for 8% of GM's stock. So far, it's a bad bet. On Oct. 17, GM showed Wall Street sharply higher third-quarter earnings, but its stock didn't budge. In fact, at \$45.75 on Oct. 18, GM shares are up just 9% on the year.



probe into health-care payments and reimbursements. The investigation, conducted by the Inspector General of the Health & Human Services Dept. and the U.S. Attorney for Massachusetts, is the feds' third probe of NMC. The company announced in April that grand juries in New Jersey and Virginia were investigating.

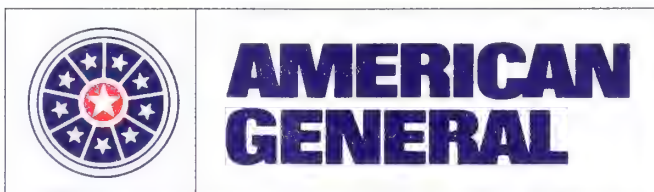
## NETWORKS: BACK IN THE BALLGAME

ONE OF THE WORST DEALS IN broadcasting history, the \$1.06 billion CBS contract to air baseball games from 1990 to 1993 managed to damage both the network and the sport. Now, both parties are trying to rebuild. Broadcasting sources say that CBS and the Fox TV network are discussing an \$880 million, four-year broadcasting partnership with Major League Baseball. But they're not

alone: As word of the deal leaked, sources say, it joined the fray. The network had forsown baseball earlier this summer, but ABC's owners at Walt Disney want a joint ESPN/ABC Baseball could have something it would not have dreamed of three weeks ago: a bidding battle could produce \$250 million a year. So far, none of the networks has ventured high. But negotiations are far from over.

## ET CETERA...

- Louisiana-Pacific will allow up to \$375 million to settle class action suits.
- Jerome York will remain at Chrysler execs—but not at Robert Eaton—on Oct. 5.
- Ivax will merge with Eli Lilly and Nycomed, creating a generic-drug giant.
- Eastman Kodak will allow back up to \$1 billion of stock. Investors rejoice.



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ED BY OWEN ULLMANN

# BOB DOLE'S BIGGEST PROBLEM IS STILL MR. UNDECIDED

These are tenuous times for Bob Dole. Just check out the Queen City Rotary Club in Manchester, N.H. At a breakfast the day after the 10 Republican Presidential wannabes made a joint appearance on Oct. 11, not one of the 30arians picked the Senate Majority Leader as their candidate. The landslide winner: undecided. "We're keeping things open," says club member Doug MacDonald.

It's a common refrain. Last spring, the Kansan looked like a sure thing to win the Republican nomination, and he made headlines in GOP fund-raising (page 34). So why are the polls so slow to commit? In two words, Bill Clinton. The

stay of Dole's campaign—that he is Clinton's strongest rival—is being undermined by polls showing him losing ground to the incumbent. And as long as Dole is vulnerable, Dole risks challenges. House Speaker Newt Gingrich (R-Tex.) and retired General Colin L. Powell (R-N.Y.) are a long way from being as charismatic as Dole, says Texas A&M University political scientist Jon R. Bond.

**BUTTONS.** That's one thing Dole has been accused of. But the Senator's campaign has other plans for turning his weaknesses around. He plans to regain the spotlight recently hijacked by Powell's megahyped book tour, Gingrich's White House musings, and Ross Perot's third-party machinations. To that, the Dole camp is looking for hot-button themes—simply the Senator's well-received assault on Hollywood values to capture headlines and define his public persona. Among the options: a call to make English the official U.S. language, playing to strong anti-immigration sentiment.

In Dole's reserve of grassroots muscle. After a embarrassing draw with Senator Phil Gramm (R-Tex.) in the August Iowa GOP Presidential straw poll, Dole's organization is hellbent on a clean win in a Florida straw poll set for Nov. 18. And he has upped the ante by making repeated

visits to the Sunshine State and personally lobbying delegates.

Dole's advisers also want to burnish his Hill leadership credentials, which have been tarnished by bitter partisan conflict, GOP infighting, and rising public disapproval of Republican priorities. "Dole has to demonstrate that he is an effective leader and can get things done," says Wichita State University political scientist James W. McKenney.

That's tricky. First, Dole hopes to appease GOP conservatives by passing a balanced-budget plan that overhauls welfare, chops Medicaid, cuts taxes, and slows the growth of Medicare. That should neutralize Gramm on the right. And

Dole knows he eventually must cut a budget deal with Clinton largely on GOP terms, so the Senate leader doesn't revive conservative charges that he's an ideology-free pragmatist. That image was reinforced on Oct. 17 when Dole admitted he erred in August by returning a \$1,000 donation from a group of gay Republicans.

**EBB AND FLOW.** Even so, if the budget battle and the Florida contest turn out well for Dole, Powell may not run—a big relief for the Kansan. An Oct. 16 poll by Manchester-based American Research

Group shows Powell whipping Dole 30% to 21% among New Hampshire Republicans. With Powell out, Dole leads his closest rival, Patrick J. Buchanan, 32% to 10%.

Dole's advisers believe his current woes are temporary—"the natural ebb and flow of a campaign" for a front-runner, says senior strategist Bill Lacy. Indeed, polls show that Dole still has bedrock support as the least objectionable Presidential candidate. "Voters are saying, 'If you can't find anyone better, we'll take him,'" explains American Research President Richard Bennett. That's no rousing endorsement. But if Dole sticks to his comeback playbook, it might be just enough to keep him on the road to the White House.

*By Richard S. Dunham in Manchester, N.H.*



**FADING?** Embarrassment in N.H.

## CAPITAL WRAPUP

### FLATTENING THE CPI

The Clinton Administration is eyeing a deal with Capitol Hill Republicans to help balance the budget by cutting annual cost-of-living hikes. Economists contend inflation is overvalued by the Consumer Price Index, which is used to adjust income tax brackets, Social Security checks, and Social Security pensions. The GOP loves the index. Why? Cutting CPI increases by one percentage point would save \$281 billion by 2002, estimates the Congressional Budget Office.

### KESSLER: STILL AT LARGE

► The regulator heading Hill Republicans' most-wanted list may elude capture—for now. The GOP had vowed to quell the Food & Drug Administration and its activist chief, David Kessler, whose alleged crimes include delaying product approvals and heavy-handed enforcement. But the budget battle and the complexity of FDA reform have forced delays. "You won't see a bill this year," admits FDA critic Representative Richard M. Burr (R-N.C.).

### CAMPAIGN SPIRITS

► Spiritual beliefs greatly impact voters' choice for President, finds a new nationwide survey. A Sept. 17-21 poll conducted by EPIC-MRA/Mitchell, based in Lansing, Mich., found Bob Dole beating Bill Clinton among those who believe in the devil (49% to 37%) and in angels (47%-40%). But Clinton coasts to victory among those who believe in reincarnation (59%-30%). "It's because Clinton keeps resurrecting himself," quips EPIC-MRA pollster Ed Sarpolus.



CANADA

# WOULD QUEBEC SURVIVE SOVEREIGNTY?

If the separatists win on Oct. 30, major economic upheaval will follow

**L**aurent Beaudoin, CEO of transportation equipment giant Bombardier Inc., trembled with emotion as he addressed a recent gathering of Montreal business leaders: If Quebec votes "*Oui*" for sovereignty on Oct. 30, he warned, the "economic disruption" would be so severe that Bombardier might have to move jobs from its factory in Valcourt, Que.—where the snowmobile was invented—to the U.S. Beaudoin's speech drew a loud ovation. But it enraged Quebec Premier Jacques Parizeau. He accused Beaudoin of "spitting in the soup" of Quebec's workers.

Referendum fever is gripping Quebec. From potluck suppers in small towns to mass rallies in Montreal, politicians, businesspeople, and ordinary citizens are debating whether Quebec should separate from Canada. The issue has pitted business against pro-sovereignty unions, Quebec's French-speaking majority against the English-speaking minority, and the separatists against the rest of Canada. Although most observers expect a *Non* victory, polls show the two sides neck-and-neck, with less than two weeks remaining before the vote. An Oct. 14 survey by Groupe Leger & Leger, Quebec's largest pollster, puts the *Oui* at 49.2% and the *Non* at 50.8%.

Quebeckers see three possible outcomes to the vote (table). If the *Non* vote wins by a solid margin—as business leaders and federalists hope—the referendum will put an end to Quebec's three-decade push for more autonomy and probably force Parizeau to resign. But a narrow win by the *Non*, with less than 55% support, could heighten tension. It would mean that a majority of French-speaking Quebeckers back sovereignty, providing ammunition for separatists to campaign for

yet another referendum and talks with Canada over a special status for Quebec.

The best the *Oui* forces can hope for is a "very, very narrow victory," says Jean-Marc Leger, President of Leger & Leger. But even with "a majority of one vote," insists Quebec Deputy Premier Bernard Landry, "that will be good enough for Quebec" to leave Canada. The province would immediately call for negotiations with Ottawa. If the *Oui* vote wins, Brian Ney-Smith, President of the Canadian Bond Rating

Service, predicts a "liquidity crisis," foreign investors stop buying Canadian bonds until the confusion settles.

Whatever the outcome, Quebec feel echoes of the debate for some time. The referendum is the culmination of separatist strength since Carle rejected Quebec's bid for autonomy in the early 1990s. Separatists won two-thirds of Quebec's seats in Parliament two years ago and provincial elections last fall. Since then, they've prepared a blueprint for independence, including a sovereignty declaration that "the t-

*Oui!*



**PUSHING HARD:**  
A loss could lead Parizeau to quit

## Three Scenarios for Quebec's Future

### IF QUEBEC VOTES "OUI" FOR SOVEREIGNTY

The province would seek negotiations with Canada on a new political and economic partnership. The hottest issue: Splitting Canada's \$450 billion in federal debts.



me to reap the fields of history." I, even many separatists concede he majority of Quebecers don't outright independence. The separatists are trying to reassure Quebecers they can vote *Oui*, yet still retain ties to Canada. Parizeau has even campaigning in a bus decorated with the Canadian dollar. The message: A sign Quebec would keep the Canadian currency. It's a stunning shift for Parizeau, who in 1984 resigned from the *Québécois* when it temporarily gave independence.

**DEATH.** In an even more remarkable concession, Parizeau on Oct. 7 effectively handed over leadership of the campaign to his arch-rival, Lucien Bouchard, head of the Bloc Québécois, federal wing of the separatist cause. Bouchard electrified the flagging *Oui* campaign. Polls show that Bouchard is the politician Quebecers most trust. His popularity has soared since he lost a leg to a rare bacteria last December, narrowly escaping death. Bouchard is now assuring Quebecers he will forge a new partnership with Canada as Quebec's "chief negotiator" following an *Oui* vote. The aim would be to create a new Canadian union over-

seen by a Parliament of elected officials from both countries. Bouchard is a potent salesman for a "courageous" *Oui* vote. "We have no right to waste another Quebec generation on sterile debates," he says.

In an ironic shift, it's the federalists who are talking about independence. They've blanketed Quebec with signs warning that a *Oui* would inevitably

## As separatists promise close ties with Canada, federalists warn of total exile

mean separation from Canada. That has been backed by warnings from politicians across Canada. Quebec's "partnership proposal is a nonstarter," Ontario Premier Mike Harris told a cheering crowd at the Canadian Club of Toronto on Oct. 12. "A separate Quebec would be a foreign country, period."

At a recent federalist rally in a shopping mall north of Montreal, that message was conveyed in personal terms. If

Quebec votes *Oui*, a *Non* organizer warned, citizens would be stripped of "the world's most envied passport." That prospect terrifies Quebec immigrants and the English-speaking minority, despite separatist promises that they could keep their Canadian passports. Pollster Leger predicts more than 90% of immigrants and English-speakers will vote *Non*. They make up about 17% of Quebec's 5 million voters.

In sharp contrast, *Oui* supporters are all Francophones. Many are prosperous and well-educated professionals, like Gaetan Perrault from Charny, near Quebec City, recently retired as a middle manager for Xerox Canada Inc. "Quebec would be better off on its own," Perrault reasons, "since we could eliminate" a whole layer of government. The *Oui* is also backed by baby boomers, who fell in love with the cause in the '60s.

With about 40% of the voters firmly committed, the outcome hinges on the 15% to 20% who remain undecided. Many voters, though Quebec nationalists, are concerned about the economic consequences of a *Oui* vote. That concern should play into the hands of the federalists. "Separation [would be] extremely

expensive for Quebec," warns the Toronto-based Dominion Bond Rating Service. The new country would be burdened by a crushing debt load, forcing it to get serious about containing its budget deficit. Spending cuts would further depress the anemic economy, where unemployment is already 10.9%. Meanwhile, U.S.-Quebec trade—worth \$34 billion last year—would take a beating while Quebec applied for admission to NAFTA.

Business is almost unanimously on the *Non* side. "We would lose a lot of business if this goes through," says Gordon Pozer, who operates a trucking company with some 40 employees in Saint-Georges de Beauce, on the Maine border. If Quebec separates, many small companies would leave the province. Bigger groups such as Air Canada might move their headquarters from Montreal.

If Quebecers vote with their heads on Oct. 30, the *Non* should prevail. But separatism is also an appeal to the heart of a people who feel they've never gotten their due in Canada. No one is better than Lucien Bouchard at invoking this romantic legacy. If he works his magic, the vote on Canada's future could prove historic.

*By William C. Symonds in Montreal*



**QUEBEC VOTES "NON" BY A NARROW MARGIN**

**IF QUEBEC VOTES "NON" BY A STRONG MARGIN**

its will declare a moral step up their campaign to concessions from Canada, and prepare for another

The sovereignty movement will be crippled and the issue shelved for a decade or more, forcing Quebec to address its economic problems.

DATA BUSINESS WEEK



## FRANCE

### CAN GEORGE CROSS AN OCEAN?

JFK Jr.'s new toy could be the next magazine Hachette clones

**S**ince its strategy is to spawn magazines it can clone worldwide, it's curious that French publisher Hachette Filipacchi Presse would bankroll *George*. This glitzy new bimonthly on the inner thoughts and personal lifestyles of U.S. politicians seems as American as a Martha's Vineyard clam-bake. Moreover, many experts doubt the *George* concept can work even in the U.S. Founder John F. Kennedy Jr. saw his idea rejected by several American publishers before he turned to France's largest magazine group last summer.

Hachette's president, Gerald de Roquemaurel, admits he, too, was skeptical at first. But Kennedy was persuasive. Now, de Roquemaurel is happy with *George*'s inaugural issue, dated October, which sold out its 560,000 copies and was stuffed with yuppie ads from Gucci, Armani, and Guess. And true to Hachette's core strategy, de Roquemaurel may yet export the concept, as it's doing with *Elle*, *Woman's Day*, and other titles. In Europe as in the U.S., explains de Roquemaurel, "politics is based less and less on philosophies, and more on personalities."

**EXPERIMENT.** Besides, *George* won't make or break Hachette. The projected cost of the magazine's launch approaches \$20 million, hefty but still affordable for a company with sales of \$1.7 billion. Hachette claims to be the world's largest magazine publisher, based on number of titles—138—and total circulation—680 million.

Hachette's high-profile experiment with *George* is a sign of the French company's growing importance in the U.S. market, where its profits are so strong they are fueling a global drive. Just a few years ago, though, Hachette's image was in tatters. To grow beyond France, it paid a rich \$712 million in 1988 for the U.S. magazine empire of Diamandis Publications: *Woman's Day*,

*Car & Driver*, and photo and stereo magazines. Recession and the gulf war quickly slashed advertising, while heavy debt squeezed Hachette's profits. The French company tried to sell *Woman's Day* but failed, scaring advertisers away in the process.



#### HACHETTE'S GLOBAL STRATEGY

##### DOMINATE KEY CATEGORIES

Hachette titles such as *Elle*, *Femme*, *Road & Track*, and *Woman's Day* are major players in their French and U.S. markets.

##### SEEK OUT LOCAL PARTNERS

Ventures with John Kennedy Jr. (*George*) and financier Ron Perelman (*Premiere*) help attract new ideas and cut costs.

##### ROLL OUT TITLES WORLDWIDE

*Elle* and *Car & Driver* now appear in local languages in Asia and Europe. *Premiere* may go global.

DATA BUSINESS WEEK

Now, Hachette's U.S. boss, David J. Pecker, has made its American magazines Hachette's crown jewels. In ad pages, *Woman's Day* has risen to the top of the "seven sisters" of women's magazines. *Elle* has pulled out of a slump. In contrast, Hachette's French titles—*Elle*, *Femme*, *Tennis*, *Top Model*, and others—currently suffer from an ad recession at home. Analyst Olivier Fèvre of NatWest Sellier in Paris thinks the U.S. now produces two-thirds of Hachette's profits. The publisher's earn-

ings hit \$77 million last year, vs. \$3 million in 1992, the year Hachette structured as a joint venture with French partner Filipacchi Medias.

Hachette hopes to boost profits by sticking to the cloning strategy it used with *Elle*, which appears in separate editions in 26 countries and 17 languages. A South African *Elle* will debut next year, with Mideast editions to follow. "It's a great way to spread your costs," says de Roquemaurel.

**"DEMISTIFIES POLITICS."** Thus, *Car & Driver* has new editions in Greece, Hong Kong, and Spain. In China, where a rising middle class lacks practical women's magazines, Hachette has launched a version of *Woman's Day*; Hong Kong and Taiwan may come next. Clones contain local articles, as well as pickups from Paris or New York. *Premiere*, the entertainment magazine Hachette bought

jointly with Revlon,

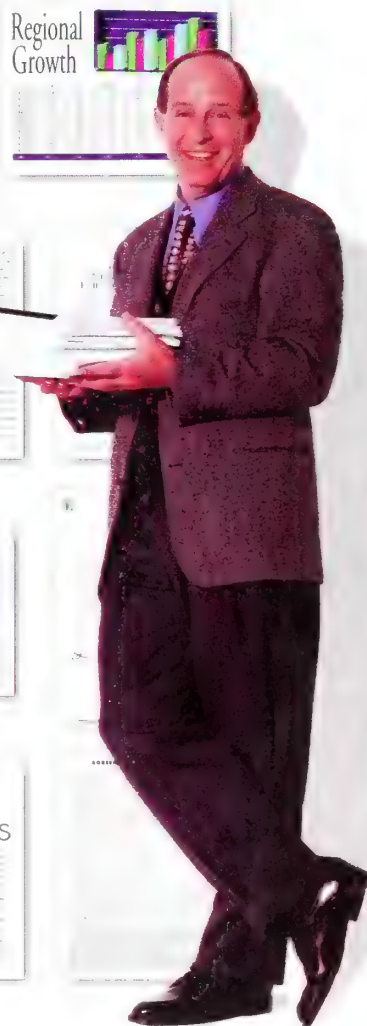
Ron Perelman could soon fuel the global curiosity about Hollywood dream factories.

Whether *George* is next in foreign kiosks depends on the niche it develops in the U.S. after an initial hoopla fades. Judgments vary. Andrews, director of print buying at Codan PLC's Zenith Media Services, complains

there's "not a lot of compelling reading." But Paula Brooks, managing partner for media services at advertising Margeottes Fertitta & Partners, defends *George* as an "interesting" magazine that "demystifies politics." She bought space in the first issue and is buying more. "There's some concern John [Kennedy] will lose interest," Brooks says, "but none that Hachette will."

Indeed, Hachette is delighted that *George*'s first issue drew a fat 170,000 pages, and even happier that its No. 2, due out in December, already has 180. De Roquemaurel hopes *George* will continue the tradition of U.S. magazines spawning French copies: *Life* to *Paris Match*, *Time* to *L'Express*, *Playboy* to *Lui*. So far, he can't think of a French name to replace *George*, which refers to America's first President. Orvis? Charlemagne? Probably he needn't rush. Media experts say *George* may thrive for at least six issues to prove that politics sells.

By Stewart Toy in Paris, with Christopher Power in New York



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**SOUTH KOREA**

## SEOUL YANKS THE CHAEBOL'S LEASH

A sudden policy shift could slow investment abroad

On Oct. 10, Queen Elizabeth II and Samsung group Chairman Lee Kun-Hee pulled ceremonial levers to officially open a \$700 million microwave and PC monitor plant in Britain. It is South Korea's single largest investment in Europe. Determined to become even more global, Lee has plans to invest \$4 billion in China for electronics and \$2 billion in the U.S. to make semiconductors and other products. All of Korea's top four *chaebol* have similar visions of rapid international expansion.

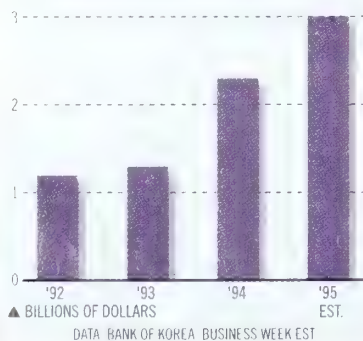
But something may be happening on the way to globalization. Also on Oct. 10, after years of encouraging the *chaebol* to go international, the government of President Kim Young Sam signaled a sharp change of course. In effect, it is now trying to slow the rush by changing the way the companies finance offshore deals. Some of the planned investments could be stalled or postponed indefinitely.

The big question is why the change of heart. The official explanation was concern about *chaebol* borrowing too much money abroad, thus raising Korea's \$70 billion debt. But another reason seems to be emerging. Key bureaucrats at the Finance & Economy Ministry grew worried that the offshore push would hollow out South Korean industry just when it might be called upon to play a role in re-

unification with communist North Korea.

The top *chaebol*—Daewoo, LG Group, Hyundai, and Samsung—had recently announced plans to invest at least \$20 billion overseas in the next five years. The scale of these plans triggered fears that a transfer of production from Korea could undermine economic reunification with the North. "We must mobilize all our resources at this time, so that if there is a serious crisis or chaos in North Korea, we've got the means to deal with it," says a senior government official. Pyongyang is currently grappling with flooding and rice shortages.

### KOREA'S DIRECT FOREIGN INVESTMENT SOARS



**MONEY PIT?** At home, Samsung faces steep labor costs and interest rates

The technique the government is using to slow down investment is to require all South Korean companies making investments of \$100 million or more to obtain at least 20% of the capital from inside Korea. Because interest rates in Korea are around 12%, the effect is to make it more difficult, and expensive, to raise capital. Some investors applaud the move. "It will help the companies' financial health," says John Lee, lead portfolio manager for the \$8 million Korea Fund. "Already, Korean companies are highly leveraged."

But corporate chieftains aren't buying it. They say they must establish global presences as quickly as possible to remain competitive. "Without globalization of our operations, we cannot grow as much as we would like," says Kim Young-Jun, executive vice-president of LG Electronics, which just acquired a 57% stake in Zenith Electronics Corp. **DAEWOO WOES?** The need to go global stems from an increase in costs inside Korea, particularly for labor. "We cannot do business anymore in Korea," says Hyundai group Chairman Chung S. Yung, who in early October announced a \$4.5 billion plan to invest overseas.

Which foreign investments will proceed? Analysts say companies such as Samsung Electronics and Hyundai Electronics Industries, with massive cash flows from semiconductor sales, should have no difficulty financing their \$1 billion semiconductor plants in Texas and Oregon, respectively. LG Electronics for its \$350 million investment in Zenith is tapping the reserves of its LG Semicon unit for \$70 million. The rest will be raised in Hong Kong's stock market.

Daewoo could face the greatest difficulties because its plans are the most ambitious. It wants to build 1 million cars by 2000 in countries including India, China, Poland, and Uzbekistan. Two major projects on the table: the takeover of a car plant and a truck plant in Poland, each for \$1 billion. It is competing against General Motors for one of them.

Daewoo executives are tight-lipped about how they will respond to the government's new policy. But it's possible *chaebol* executives will resort to more offshore fund-raising techniques to circumvent government control. That could deepen the conflict with elite bureaucrats over just how far economic liberalization can proceed at a time when the prospect of a North Korean meltdown seems to be growing.

By Laxmi Nakarmi in Seoul

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## BRAZIL

### 'WHAT HAPPENED IN MEXICO... COULD NEVER HAPPEN IN BRAZIL'

A talk with President Fernando Henrique Cardoso

**B**razil's dizzy inflation has slowed to less than 1% a month, and gross domestic product is growing at around 5% this year under the anti-inflationary Real Plan launched in 1994 by then-Finance Minister Fernando Henrique Cardoso. Its success helped Cardoso win election as Brazil's President last fall. Now, he is carrying out an even harder task: mobilizing support for deeper free-market and social reforms—in a diverse nation of 160 million and an often-fractionious Congress. In his office in Brasília on Oct. 13, Cardoso discussed his leadership style and why he thinks Brazil's reforms are unstoppable, in an interview with *BUSINESS WEEK's* São Paulo correspondent, Ian Katz.

**Q:** How do you convince the skeptics, particularly since Mexico's crisis, that Brazil will push ahead with reforms?

**A:** We are making all our changes within a democratic system in a very open way. What happened in Mexico—where people didn't know the real state of the economy—could never happen in Brazil. Here, everybody knows everything: The press is very active, business groups are strong, and the Congress analyzes. The reform process is irreversible because the population accepted this new way of doing things. There are not only a lot of economic differences between us and Mexico but our societies are also very different in political culture and decision-making. There are no secrets in Brazil.

**Q:** Has your experience as a sociologist and teacher at American univer-

sities shaped how you do your job?

**A:** The most important decision I made as Finance Minister was to explain the stabilization program to the country. That's because I'm a sociologist, not an economist. Until lately, all decisions were made technocratically. In a democratic society, a leader has to motivate the people and explain.

When I first went to the U.S. more than 30 years ago, I realized that Bra-



**CLOWNING WITH THE BOYS:** Cardoso's pushing for better schools

zil was an American-like country. I was surprised because I felt close to São Paulo in New York. The Brazilian state, with its former empire and bureaucracy, is maybe more European. But the society—the grassroots movements, the tendency to decentralize, and a certain individualism—is more American.

**Q:** How do you get reforms enacted?

**A:** The Congress is fragmented, and each party is fragmented. The difference between President Clinton and me is that he has an organized majority against him and I have a disorganized majority in favor. I can get

things passed, but I have to participate actively and use consensus to push things.

**Q:** How does your style compare with other Latin American leaders?

**A:** [Peruvian President Alberto] Fujimori is more charismatic: He sits with the flag. That works symbolically because nowadays a President has to have a symbolic role, too. [Argentinian President Carlos] Menem is different. He allows [Economy Minister Domingo] Cavallo a lot of presence—as Menem handled the politics and Cavallo the administration of the economy, even though Menem is in charge. There's nobody here like Cavallo. I'm not much of a detailist, but I'm a hands-off, either.

**Q:** What are the biggest remaining obstacles to making reforms?

**A:** Some sectors of state-run companies: They have an antiquated view of Brazil as an autocracy. And the traditional clientelism—people who depend on the state. It's not a legal right issue. These are cultural obstacles. The bulk of business is backing the reforms. Union leaders are divided but are moving ahead. The Church is divided because of ideological perceptions. In Congress, some people are against us, but they're not proposing alternatives. Without alternatives, it's difficult to support the status quo.

**Q:** What are you doing to narrow Brazil's huge gap between the rich and the poor?

**A:** The Real Plan has brought about the greatest income redistribution: It stopped the "inflation tax." Consumption has increased a lot. Improving education is another instrument for redistribution, but it takes 10 years. In technology, the private sector is investing more than \$1 billion [over three years] thanks to incentives [such as tax breaks for plant upgrades]. In a year, all you can do is what I've done—change course.

President Clinton "has an organized majority against him, and I have a disorganized majority in favor"



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## WALESA MAY FINALLY HAVE WORN OUT HIS WELCOME

**P**oland without Lech Walesa as President? It's hard to imagine. The electrician who led the Solidarity trade union against the communists has been a constant, if controversial, fixture in Polish politics for 15 years. But with the first round of presidential elections slated for Nov. 5, he could get the boot.

While Walesa remains a powerful symbol to outsiders, many Poles think he has overstayed his time. They have grown weary of his incessant grandstanding and infighting, which disrupts government. His shrill anti-communist message makes it hard for the country to bury its troubled past and edge itself toward a more secure political and economic footing. "Poland needs some fresh blood," says Jerzy Wilkin, an economist at Warsaw University.

**BEST ASSET?** The immediate problem for Walesa is that, unless someone wins 51% of the vote, only two of the 17 candidates will survive the first round, and he may not be one of them. The main leftist candidate, Aleksander Kwasniewski, party chief of the ruling Democratic Left Alliance (SLD), a group of former communists and other leftists, seems certain to get through. Walesa also faces challenges from Hanna Gronkiewicz-Waltz, president of the central bank and a vocal Catholic; Jacek Kuron, one of the most popular folk heroes of the Solidarity revolution; and civil rights ombudsman Tadeusz Zieliński. Walesa is particularly worried about Gronkiewicz-Waltz, whom he appointed to the bank. He has recently resorted to calling her a "hyena" and other names. She counters that Walesa uses people and then throws them away.

Ironically, Walesa's best asset may be fear of Kwasniewski, an articulate 41-year-old who served as a junior minister under the communists. Kwasniewski has done a creditable job as leader of the largest parliamentary bloc and thus as one of Poland's key powerbrokers. The smooth politician, who fancies

himself a young, charismatic leader in the John F. Kennedy mold, proved his reform credentials by supporting Walesa dumping the foot-dragging Prime Minister Waldemar Pawlak last spring. He also helped kick-start the long-delayed privatization program. Such moves have foreign investment on the rise, and Poland's gross domestic product growth this year could hit 6%—tops in Europe. By contrast, Walesa, hoping to win some votes, recently vetoed a pension reform plan that would have saved the treasury \$2 billion.



**POWERFUL SYMBOL:** But shrill

**MASS APPEAL.** But many Poles still worry about turning over too much power to a former communist. Investors, too, could get the jitters if Kwasniewski wins. The Catholic church, which claims 90% of Poles, is whipping up fears of a return to the Dark Ages. Bishops are issuing dire warnings not to vote for ex-communists. Walesa has been playing along, ostentatiously attending mass around the country. In such an atmosphere, Walesa, irritating as he may be, looks to be the best protection. That is probably why he has edged ahead of his rivals in the center-right in recent polls.

If the final vote, to be held on Nov. 18, boils down to a Kwasniewski-Walesa fight, there could be unfortunate consequences for Poland. Such a pairing is likely to generate the rawest of emotions at a time when the country would be better off minimizing the old conflicts. Some of Walesa's rivals, such as Kuron or Gronkiewicz-Waltz, have the clout and flexibility to broker deals between the descendants of Solidarity and their communist adversaries. Walesa was the right man to lead the dismantling of communism; he stays on, he'll have to either develop the more subtle skills required in the late 1990s or risk undoing what he has achieved.

*By Karen Lowry Miller in Boston  
with Peggy Simpson in Warsaw*

## GLOBAL WRAPUP

### FRANCE: MORE BAD NEWS

► The troubles of French President Jacques Chirac are deepening. As terrorists—probably from Algeria—exploded the eighth bomb since July in a Paris subway on Oct. 17, a new corruption probe threatened the job of Economics Minister Jean Arthuis. Named less than two months ago to succeed Alain Madelin, who was fired for preaching fiscal rigor, Arthuis is suspected of illegally funding his small center-right party. Meanwhile, France's economy is slowing. Tax rev-

enues, the bourse, and the franc are falling. So is the approval rating of Prime Minister Alain Juppé—now just 32%. Chirac, in power since May, may be pressured to dump Juppé and make a fresh start.

### WESTINGHOUSE SETTLES

► After an acrimonious seven-year legal battle over a stalled nuclear plant, Westinghouse Electric is paying the government of the Philippines \$100 million in cash and equipment to settle the dispute. But the chief beneficiary of Westinghouse's deal is a com-

petitor, Mitsubishi Heavy Industries. The Filipinos had barred Mitsubishi from a separate \$1.4 billion power contract because of the company's use of Westinghouse-licensed technology. So Mitsubishi pressed Westinghouse to end its fight. Now Mitsubishi is likely to reel in the power contract while Westinghouse takes a hit.

The deal in Manila clears a cloud from Westinghouse. And it positions Westinghouse's power generation unit for possible sale, as the company raises cash for the \$5 billion CBS buyout. A possible buyer? Mitsubishi.

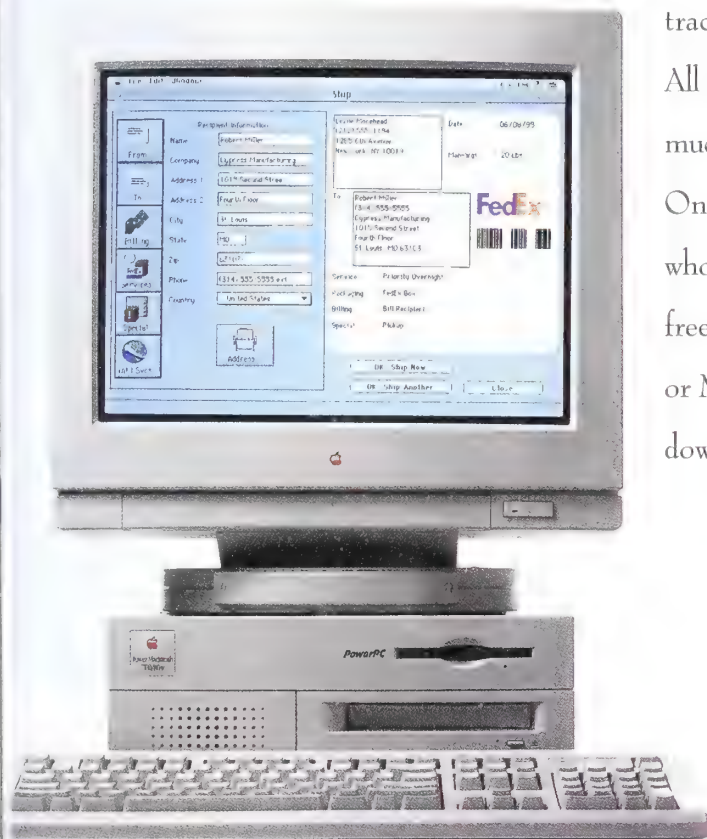
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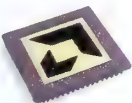
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# WELCOME TO THE WORLD WIDE LAB

By providing instant access to data, the Web is changing how research is done and shared

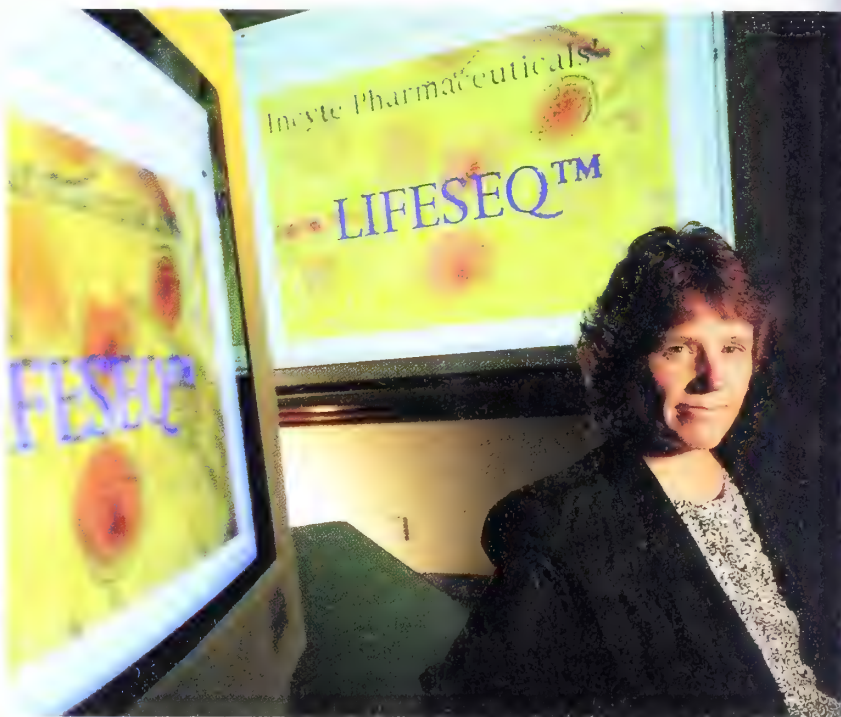
**D**r. Ingrid E. Akerblom's research at Incyte Pharmaceuticals Inc. could be crucial to developing a new generation of superior medicines. But this biologist never peers into a microscope, squints at a lab rat, or draws blood from a wincing patient.

Rather, Akerblom sits at a computer all day, analyzing genetic information that will be part of a giant database program linked to information sources around the globe. Her job is to make those data sing. With a few mouse clicks, she can zip from her Palo Alto (Calif.) headquarters to Switzerland, Washington, and St. Louis, amassing clues about disease pathology, for example, that just a few years ago would have taken months to harvest from traditional biology experiments and days to cross-check in the bowels of a library.

Although she is glued to a powerful workstation, Akerblom bears little resemblance to the "digital scientists" who drive the world's fastest supercomputers to model cosmic string theory and other exotica. While these pioneers rule the theoretical reaches, Akerblom is part of a more grassroots phenomenon: scientists using the ever expanding graphical and software links of the World Wide Web as a new way to do science.

The potential of the Web, created by physicists less than five years ago to speed navigation of the global Internet, is tantalizing scientists of nearly every persuasion and changing the way they run experiments, compare data, and publish papers. It's also leveling scientific hierarchies by giving researchers around the planet access to the most advanced scientific tools and databases. The Net may not be ready for prime-time commerce, as recent security breaches suggest. But it is becoming a surprisingly powerful platform for scientific discovery. Says San Diego Supercomputer Center computational ecologist Richard Marciano: "The scope and magnitude of problems being tackled is at a level never reached before."

Incyte's crown jewel is Lifeseq—a pro-



**GENE-CRUNCHING:** Web links give Akerblom data from St. Louis to Switzerland

proprietary database holding tens of thousands of gene sequences extracted from tissue libraries. Trouble is, each sequence is just a long stream of raw genetic code—alphabet soup, to the naked eye. Incyte and its pharmaceutical partners, including Upjohn, Novo Nordisk, Pfizer, and Hoechst, seek answers to specific questions, such as which genes are turned on in cancer, or what effect a chemical has on genes linked to arthritis.

**NATURE'S CODE.** To create signposts, Akerblom and other Incyte researchers "annotate" gene data as they arrive and use HTML (hypertext markup language)—the link-building programming language of the Web. By using the Netscape Communications Corp. Web browser, scientists can explore connections, say, between lists of genes functioning in healthy vs. diseased tissue. And they can step seamlessly from Incyte's private domain to public databases. The

possibilities that open up, Akerblom says, "have blown my scientific mind."

The exponential increase in data from the Human Genome Project is one factor driving biology to the forefront of Web-based science. DNA is as close as nature gets to pure software code and is readily adapted to computer analysis. As a result, experimental biology has evolved from in vitro and in vivo to "in silico." GenBank, a public, Bethesda (Md.)-based gene repository, lets Web-wise scientists compare new sequence data against a huge database. The number of "intellectual queries" from the Web has soared from zero in 1992 to 12,500 a day now. Earlier this year, researchers using the query approach to study the so-called ataxia gene were thrilled to uncover a similar gene in yeast—one that has been studied extensively. That provided hints to the human gene's function. In a matter of seconds, says GenBank Director

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**Why pay to repair a used vehicle when you could be driving a new one?** After 30,000 miles you may have to start making routine replacement of wear items such as brakes and tires. With a 24-month Red Carpet Lease, you'll be into a new vehicle by then.

**No return fees with a Red Carpet Lease.** Some competitors' leases require you to pay several

hundred dollars just to return the vehicle at the conclusion of your lease. A Red Carpet Lease has no such fees.

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**A 24-month Red Carpet Lease has clear advantages.** As you can see, a 36-month lease with "low" payments may be too good to be true. When you look at the actual cost of driving, a 24-month Red Carpet Lease is a genuine value.

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David Lipman, the Web lets scientists "make discoveries that nobody who created the databases ever dreamed of."

Physicists, who have strong stomachs for the arcane codes of the Internet, were among the first to cruise databases and public servers. They set up the first "pre-print servers" to make scientific papers available long before they are physically published—a trend that's now spreading to other disciplines. And physicist Philip Berners-Lee invented the Web and HTML.

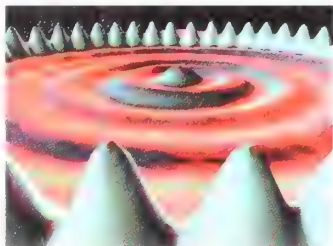
At first, researchers at the Stanford Linear Accelerator Center (SLAC) in Menlo Park, Calif., and elsewhere used Web pages for "housekeeping" chores, such as maintaining phone directories. Then some began putting up their workbooks, giving other high-energy physicists almost real-time access to notes on cutting-edge experiments.

**BAY WATCH.** When scientists in other fields saw how easy it was to navigate databases using HTML, lightbulbs went on. At the San Diego Supercomputer Center, for example, ecologist Marciano is dusting off 20 years of Landsat data sitting in tape reels and getting them Web-ready so researchers grappling with global warming, land-use patterns, or water-storage problems will be able to analyze measurements over time.

Another effort, the "San Diego Bay Project," is linking disparate databases full of measurements on sediment chemistry, bird species, and vegetation growth. Using new software tools such as Virtual Reality Modeling Language, researchers will be able to move through 3-D representations of these data.

Such powers have attracted major scientific journals, virtually all of which have gone online or are thinking about it. Neither the review boards nor most readers are in a hurry to weaken the peer review pro-

## How Scientists Are Working the Web



### REMOTE CONTROL

Scientists could one day "drive" IBM's scanning tunneling microscopes remotely to build atomic landscapes. But technicians would still load samples by hand

through, say, Stonehenge on a midsummer's day, showing the sun and shadows from the astronomically correct angles.

And since cyberspace is not bound by physical page lengths, scientists can put up their complete data so colleagues can perform their own analyses. These data are neither better nor worse in quality than they have ever been. They're simply easier to obtain. Says organic chemist Henry Rzepa of London's Imperial College of Science, Technology & Medicine: "We're trying to strip off the grime" of misinterpretation that can occur when data are marshalled to support a theory. Collaboration also takes on new resonance. Rzepa recently hosted a chemistry "conference" exclusively on the Web, including presentations, papers, and discussions—at almost no cost.

Such efficiencies are critical in a time of shrinking budgets. More and more conferences include an electronic repository for the pounds of written materials and papers scientists used to collect and lug around. And if a

meeting is hot, says Marciano, "discussions live on long after the meeting."

Even bigger cost-savers may be ahead. Last March, a group of fusion scientists joined a novel experiment at Massachusetts Institute of Technology. The sat well beyond the requisite 70-foot safety distance from MIT's Tokamak magnetic-chamber plasma device—3,000 miles beyond it, in fact, since they operated the Tokamak remotely from California.

**PLASMA DONATION.** For 12 hours Lawrence Livermore National Laboratory scientists controlled plasma bursts in the \$30 million Tokamak over the Internet, while watching the results as swapping ideas through live audio and video feeds. Scientists are studying Web-based interfaces for similar experiments. And since most major labs are facing dire budget cuts, such collaborations will likely be used to stretch scarce funding, says Ian Hutchinson, director of the Fusion Project at MIT's Plasma Fusion Center. In theory, nothing would prevent sites around the country from simultaneously viewing a fusion experiment and taking turns "driving" it. Scientists could share other resources, such as accelerators and radio telescopes.

Scientists face some of the same hurdles as business executives who embrace the Web, such as security access times, a vulnerability to corruption or sabotage. Maintaining databases is also expensive, so the best ones are often overloaded.

What's more, the sociology of science is changing. "Access is no longer a function of where you are or what your facilities are," says Bebo White, the "Webmaster" at Stanford's SLAC. By simply clicking to the home page of Pedro Coutinho, a chemical engineering graduate student at Iowa State University, anyone can browse a treasure trove of biotech resources and find pointers to powerful gene-analysis programs.

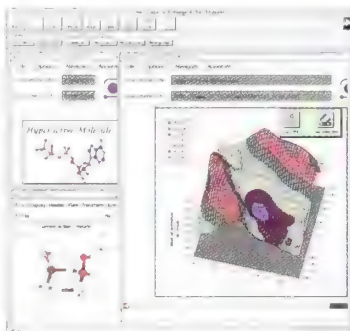
It's not surprising that such a long list of issues would arise from such fundamental development. From astronomy to zoology, scientists are putting their imaginations to work on the Web and in the process, blowing their minds.

By Joan O'C. Hamilton in San Francisco, with Heidi Dawley in London



### NEW VIEWS

Projects in chemistry, physics, and medicine exploit the Web's dazzling 3-D graphics. The National Library of Medicine sponsored digital training videos linked to these icons



### COMMUNICATIONS

Organic chemist Henry Rzepa and Britain's Royal Society of Chemistry collaborate in electronic publishing experiments to bring 3-D renderings of molecules to life

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## PROTEINS WITH AN ANCHOR FOR ENZYMES

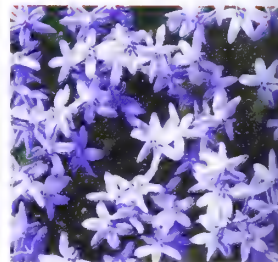
**BREAKING DOWN CELLULOSE** is one of the most vital tricks of the microbial world. Thanks to the enzymes wielded by bacteria and fungi, cows digest grass, fallen trees decay, and companies can transform corn into ethanol. But University of Rochester microbiologist David Wu has long suspected that some bacteria are far better at breaking down cellulose than their enzymes

would suggest. These particular superbugs, he discovered, harbor another protein—one that somehow boosts the efficiency of cellulose-eating enzymes.

Now, Wu and an international band of scientists have deciphered the gene that codes for this protein—and turned up a surprise. Built into the huge protein are nine sections that bind to the enzyme. This “anchorage” protein thus bris-

tles with nine copies of the enzyme, enabling it to cut a wide swath through cellulose-laden material. “I don’t think anyone ever imagined that enzymes worked this way,” says Wu.

Next, Wu will try to put the discovery to use. One idea: creating proteins for attaching enzymes that do more than just gobble cellulose. Such anchorage proteins might boost the efficiency of enzyme-containing detergents or industrial processes.



## INNOVATIONS

■ Just days apart, two teams of biotech researchers announced they had found the gene that regulates flowering. Scientists at the Salk Institute in La Jolla, Calif., and the University of California at San Diego say that the results promise to boost crop yields by coaxing plants to bloom faster and to shorten the time it takes to crossbreed new hybrid strains. They could even be used to inspire rose plants to sprout flowers where leaves would normally grow.

■ Snapshots of atomic structures have led to many new insights in materials science. But the static images that are produced by a scanning tunneling microscope (STM) don’t illuminate what happens while one atom is reacting with others. Now, physicist Brian S. Swartzentrub at Sandia National Laboratories has developed a new STM—one that’s so sensitive it can track a moving atom. It should yield new understandings in semiconductor physics.

■ Grinding the high-quality lenses used in cameras, fax machines, and smart-bomb “eyes” has always been more art than science. Until now. Researchers at the University of Rochester have devised a program that predicts the results of grinding various glass formulations. It’s a “significant breakthrough” in controlling factory-floor operations, says Harvey Pollicove, director of Rochester’s Center for Optics Manufacturing.

## SIFTING THROUGH DATA WITH A NEURAL NET

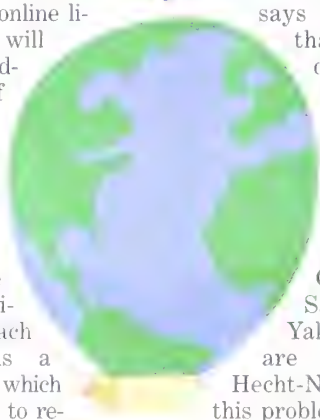
IMAGINE COMPRESSING TV pictures and high-fidelity music so tightly that they could travel simultaneously over ordinary phone lines. Robert Hecht-Nielsen, chief scientist at HNC Software Inc. in San Diego, thinks he’s on the track of just such a breakthrough—using so-called neural networks. These are brainlike circuits that learn from experience and don’t need conventional programming.

Hecht-Nielsen, a neural-net pioneer, says the technology may be the ultimate data-compression method. Laying out the math in the Sept. 28

issue of *Science*, he shows that neural networks learn to squeeze data down to the irreducible minimum. The neural net can be fed billions of bits of data—all the pixels in all the frames of a movie or all the text in an online library—and it will generate a cloud-like map of points. Because these points exist in a world of higher mathematics with an almost infinite number of dimensions, each point contains a wealth of data, which the net can use to re-

constitute every detail of the original information.

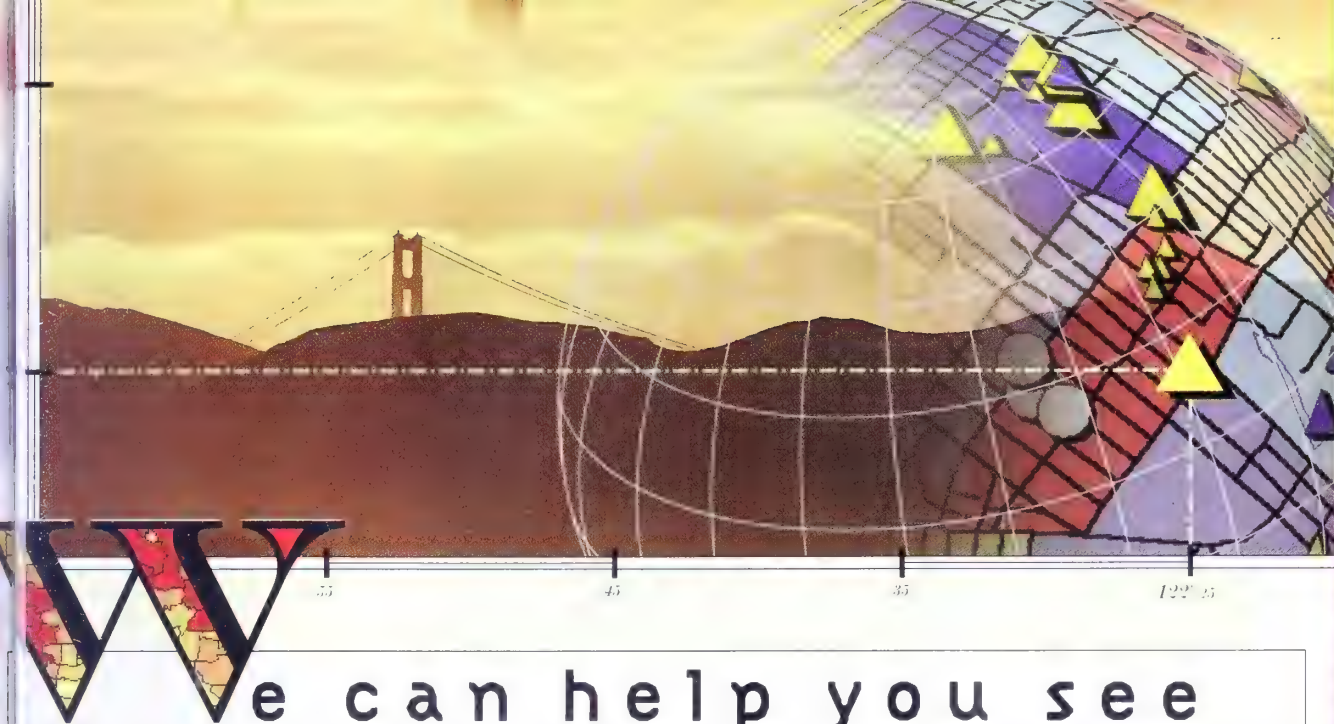
For now, there’s a hang-up when it comes to real-world applications: The neural net that produces optimum results is very complex. So much so, says Hecht-Nielsen, that “we really don’t know the best way to train these circuits.” Researchers at AT&T Bell Laboratories, the University of California at San Diego, and Yale University are joining with Hecht-Nielsen to tackle this problem.



## FOR A COOL TOOL, TRY LASERS

**STAR WARS SCIENTISTS** AT LOS ALAMOS National Laboratory are turning death rays into—would you believe?—refrigerators. Normally, lasers zap their targets with heat and can even melt solid steel. So how can a laser cool something? By tuning the laser beam so its energy “excites” the target’s atoms in a special, quantum-mechanical way. This causes the atoms to emit fluorescent light, and since the emitted radiation contains more energy than was absorbed from the laser, the target loses energy and becomes cooler.

The theory of “optical refrigeration” has been around since 1929. Now, a Los Alamos team headed by physicist Richard I. Epstein reports in the Oct. 12 issue of *Nature* that the idea is not only possible but feasible. In fact, Epstein says the concept promises technology that could eventually be used to cool computer circuits to the frigid temperatures needed by superconducting materials. With superconducting circuits, computers and other electronic gear would run hundreds of times faster than today’s hardware. Los Alamos has patented the technology and is looking for help to commercialize it.



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ENTREPRENEURS

**@ THE CAFE:** Intellectual products says Christopher Zook, director of Bain & Co.'s strategy practice, who was LearningSmith's president in 1992. Smith was a young Wall Street analyst, shopping a Greenwich Village bookstore, when he got the idea for a store selling only p-

perbacks. He moved home to Boston to start Paperback Booksmith. Breaking with custom, he organized books by subject, not by publisher, and he used spotlights and inviting nooks to draw customers. After opening three more stores, he began franchising. By 1978, there were 75 Paperback Booksmiths.

**"WORST EXPERIENCE."** Soon after, the chain flamed out, filing for Chapter 11 in 1979. The problem, many say, was that Smith supplied franchisees with books even when they owed him money. Smith says he felt obligated to the franchisees, many of whom were in subpar malls. He managed to keep two stores, but bankruptcy was "the worst experience I've ever gone through." At Paperback Booksmith, he also learned that "I can do it all myself," and since then, he has hired others to help run operations.

When Smith launched Videosmith, he positioned it as "the movie buff's movie store," emphasizing classic and foreign films. Again ambience was key. Recall Sal V. Perisano, a Cybersmith director who was Videosmith's CEO: "People loved to see our 'No Smoking' sign—80-year-old Bette Davis with a cigarette dangling from her lips." Videosmith grew to 11 stores before Smith sold for an undisclosed sum to Dublin-based Xtra-vision PLC in 1989.

Two years later came LearningSmith, which he envisioned as an intellectual playground. Books, videos, software, audio tapes, games, and puzzles are grouped by subject. Smith has shrewdly linked the stores with PBS affiliates in 16 cities, beginning with Boston's WGBH, which is also an investor. Each station

# MR. SMITH GOES TO CYBERSPACE

Retailing pioneer Marshall Smith is morphing yet again

**M**arshall J. Smith hardly seems like a retailer at the cutting edge of technology. In his preferred attire of old flannels, short-sleeved shirt, and tan suede shoes, he looks more like the bookstore owner he was for nearly two decades.

His latest venture, Cambridge (Mass.)-based Cybersmith, is a sharp contrast—a sleek space defined by bright neon cable and polished wood that houses 52 computer stations, 14 with links to the Internet. Larger and more sophisticated than most "online cafés," Cybersmith—and Smith's reputation as a retailer of intellectual property—has attracted \$4 million from such investors as Harvard business school strategist Michael E. Porter and digital

evangelist Nicholas Negroponte, who is also a director.

Cybersmith, which will open a second store next month in White Plains, N.Y., is the 63-year-old Smith's fourth foray into retailing. Taken together, his ventures reflect the changing forms of information packaging. In 1961, when most booksellers disdained softcovers as insubstantial, he started Paperback Booksmith and built it into the nation's No. 3 book chain. In 1981, he launched Videosmith Inc., one of the first video rental chains, which now has 14 stores. In 1991, it was LearningSmith Inc., a multimedia bazaar that has grown to 29 stores in 12 states. "He's continually able to come up with the next marketing twist, the next retail concept in in-

## RIDING THE INFORMATION REVOLUTION

**PAPERBACK BOOKSMITH** Established in 1961. Sold paperback books. Peak revenues: \$35 million in 1978, 75 stores nationwide. Filed for Chapter 11 in 1979.

**VIDEOSMITH** Established in 1981. Video-cassette rentals. 1989 revenues: \$7 million, 11 stores. Sold in 1989 to Xtra-vision PLC.

**LEARNINGSMITH** Established in 1991. Multimedia learning products. Current revenues: more than \$40 million, 29 stores. Smith's current stake: less than 10%.

**CYBERSMITH** Established February, 1995. Rents time on 52 computer stations. Projected first-year revenues: \$1 million. Second store to open late November.

DATA: MARSHALL SMITH



royalties for the use of its name. Jack Daniel's gets on-air advertising instant recognition by PBS viewers. Other investors, led by venture capitalist Halpern Denny & Co., came on. Smith's stake was diluted to less than 10%, and in 1994 he resigned as chairman. By then, he was captivated by the online world. His son, Jed, 29, who met him up with an America Online chat, is a partner in Cybersmith. The best Internet cafés offer a handful of games, but Smith's idea was "to have one who walks in here be on a computer," says Patricia Seitz, architect of the flagship store. Customers insert credit cards into one of 52 Apple computers, videoconferencing stations, and virtual reality machines and, says Smith, "look through the looking glass." For a minute, they can sample games, movies, and CD-ROMs or try out on-line services. "Technosmiths" who offer guided tours of cyberspace also serve coffee, which accounts for nearly 10% of revenue. And while Smith uses the term "Internet café," adding that "we're selling access to technology," he reports with delight that Time magazine has named Cybersmith's "Best First Date."

**ONE MILLION?** Smith says the first Cybersmith will take in close to \$1 million in the first 12 months. With 25% of the revenue, representing "a significant part of available cash," Smith cares very much how the company performs. Given the state of cutting-edge digital gear, profits are elusive. But "don't underestimate how much money people will spend to be online," Negroponte told the board at its meeting last month.

Corporations want to be cool, too. Time Inc. and Computer Inc. have all rented Cybersmith for events, and Microsoft is part of its "Start Me Up" campaign. Windows 95 there, though the footage is not used. Still, Smith's trading post at the edge of the digital frontier seems a risky undertaking. With online services proliferating, some wonder why people leave home to log on. Says Smith: "Marshall walks close to the line on everything he does. Cybersmith is his biggest risk so far."

In his office where Smith grapples with the risk is, like Smith, decidedly low-key. His old wooden desk could belong to a country lawyer, and his computer is an aging Macintosh IIx. He keeps a collection of quotations on scraps of paper in two shoeboxes. Dipping into the collection he chooses a line from socialist poet Goldsmith to explain his business philosophy: "If I can't dance," he reads, "let's get out of my revolution."

*By Paul C. Judge  
in Cambridge, Mass.*



Clockwise from top left, that's Jack Daniel, Jess Motlow, Lem Tolley, Frank Bobo and Jess Gamble. (Jimmy's in the middle)

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# PULLING OIL FROM DAVY JONES' LOCKER

New technologies cut the cost of deep-sea production

The Gulf of Mexico was entering its heyday as an oil-producing region when Emmett M. Richardson joined Mobil Corp. 25 years ago. He helped pioneer the idea of putting production equipment on the sea floor rather than atop costly offshore steel platforms. But before the concept sank roots in the Gulf, Richardson was off to projects in the North Sea, where his work flourished. Today, the 53-year-old head of subsea research and engineering operations for Mobil is back in the U.S., convinced that offshore oil platforms—those spindly skyscrapers of the sea—are destined to play only supporting roles in the oil industry's future.

Until recently, the approach in the Gulf has been to build bigger and bigger platforms, each costing upwards of \$1 billion. These platforms house large crews and contain wellheads with complex monitoring and control equipment, as well as gear to inject liquids and gases to keep the flows moving.

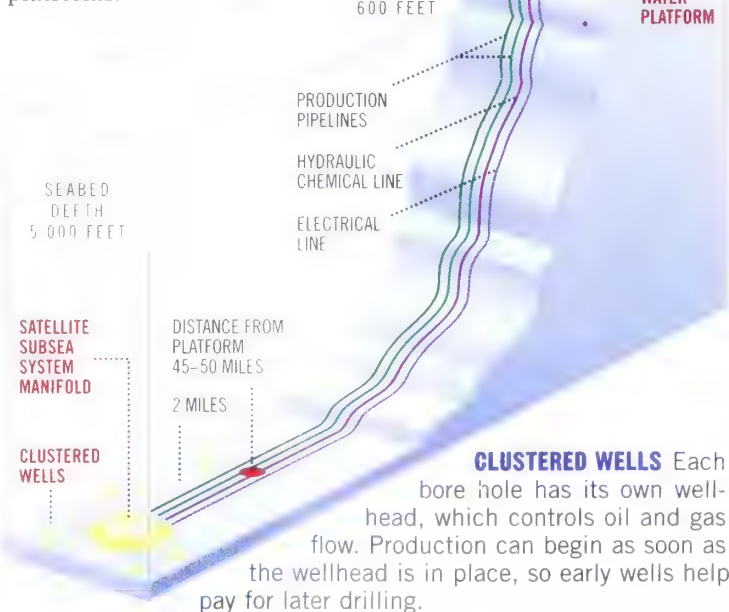
**FLOOR PLAN.** Such elaborate stations are fine in shallow waters above rich oil fields, but they don't make sense for the new fields, which are farther from shore. Big towers are difficult to anchor in deep waters, even if they are floating rather than fixed. And often, no single pocket is rich enough to warrant its own platform.

So Richardson and others are borrowing Star Wars technologies and assembly ideas to reinvent offshore production of oil and gas. The basic idea: Automate much of the

production technology and move it from the platforms to the ocean floor. Then, link up lots of these far-flung, semiautonomous wells to a central hub, or manifold. This way station then passes the wells' combined output up to a conventional offshore platform, where the oil and gas are separated from each other (illustration). One platform would then suffice for dozens of wells over hundreds of square miles.

## Plumbing The Depths

Oil companies want to cut the cost of deep-water oil and gas production in the Gulf of Mexico by placing wellheads on the ocean floor instead of on surface production platforms.



**MANIFOLDS** More adaptable than older manifolds, these hubs can gather oil and gas from wells as far as two miles away, then send the flows up to the surface.

**EXISTING SHALLOW-WATER PLATFORMS** These play a new role as way stations for the new fields. They separate the oil from the gas and send them down separate pipelines.

The long-term goal is to disperse with platforms entirely by perfecting "multiphase" pumps that can move the wells' output all the way to shore. Unlike ordinary pumps that need a platform to separate gas from the oil, these pumps don't spin out of control when they hit a gas pocket. Says Richardson: "The multiphase pump has the ability to completely change this industry."

While the multiphase pump and some other deepwater ideas are years from widespread acceptance, others are already in use. In one new project at 2,000 feet of water, Shell Oil Co. engineers connected satellite wells to a hub without divers or robotic vessels. Using a sleeve that pivots pipes into place and secures them, Shell can save \$500,000 to \$2 million per project. What's more, the hub can start delivering oil and gas as soon as the first well is connected to it. Ordinarily, all the wells, tightly grouped beneath a platform, go into production at once.

By bringing on wells one at a time, early ones generate cash that pays for later ones, says Texaco Inc. Offshore Engineering Manager J. Phil Wilbourn. Exploratory wells costing \$6 million that have been abandoned because they turn out to be too far from a platform can be hooked into a hub. Plus, the satellite method cuts risk: If a field doesn't pan out, project managers can scale the project back even after drilling has begun.

Armed with new technology, U.S. companies are venturing into ever-deeper waters. Already, 40% of proposed Gulf projects at greater than 3,000 feet of water involve the use of subsea components, says Steven Homer, a project engineer at Halliburton Co.'s Brown & Root Inc. He estimates that as many as 70% of future deepwater Gulf projects will use subsea wells tied to near-shore platforms. Worldwide, the number of so-called seabed wells should hit 185 this year, compared with just 25 in 1990, says oil industry researcher Offshore Data Services Inc.

Americans pioneered



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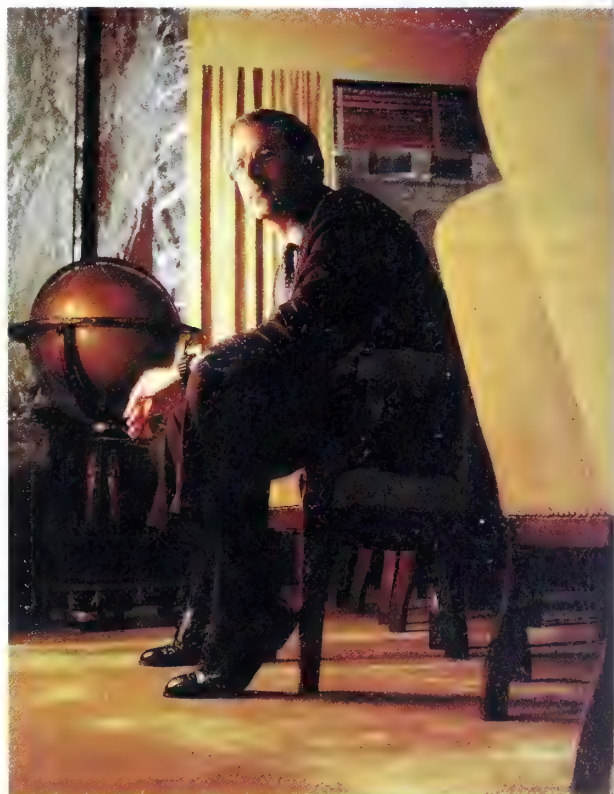
# LOST IN THE AISLES AT WOOLWORTH'S

Needed: A map to get the ailing merchant back on track

**R**oger N. Farah relaxes in the boardroom of the elegant Woolworth Building in lower Manhattan, a throwback to the glory days of the now-faltering retailer. CEO of Woolworth Corp. since December, Farah knows Wall Street is waiting for a sign he can turn the venerable merchant around. He laughs at rumors he's considering a bid to add the struggling Ann Taylor chain to Woolworth's bulging portfolio. "As soon as the business goes bad, we can have it—right?" he jokes. "I think we have some that we can sell them."

He sure does. Woolworth, weighed down by debt, antiquated technology, and a sprawling network of 40-plus specialty and variety chains—few of which make much money—has been struggling to define itself since the start of the decade. The former R. H. Macy & Co. president was brought on board to chart a course for Woolworth's confused array of businesses. The \$8.3 billion company earned just \$47 million last year, after losing a stunning \$495 million in 1993. Since his arrival, Farah has shored up the balance sheet, sold off or closed four small businesses, and recruited a new management team.

**KEEPING MUM.** What he hasn't done is convince Wall Street that he has a clear vision of where Woolworth is headed. The stock is trading around 16—about where it was when Farah was named and well below the 1992 high of 34. Investors and analysts were poised for



**NO QUICK SELL-OFFS**  
CEO since December, 1994, Farah says: "Just to dump things at this point and take a loss is not in the cards"

the new CEO to come in and clean house, but so far he has sold off little and kept mum on the subject of Woolworth's future. "The investment community is disappointed with the sales. It's moving very slowly," says Lie B. Maack, portfolio manager at Crabbe Huson Group Inc., an institutional money manager and Woolworth shareholder. Even in an extensive interview—the first in his 10 months in office—Farah said little to spell out what kind of retailer Woolworth would

subsea wells in the 1970s but largely abandoned them after running into production problems. Now, in an effort to leapfrog subsea technology pioneered by Brazil's Petrobras, Texaco is leading 17 oil producers and dozens of supply companies to advance ideas such as lightweight composite-material pipes, ultralight cables for anchoring vessels, and subsea components such as manifolds, pumps, and systems for separating oil from gas.

U.S. researchers are also working on a superfast welding technique that's ideal for composite-material pipes. A spin-off of Star Wars missile-zapping research, "homopolar" welding generates thousands of amps at very low voltage. By precisely controlling the rise and fall of the current and applying pressure at the joints, it can fuse a 12-inch pipe in seconds, compared with 20 minutes by conventional welding, says Richard J. Seymour, director of the Offshore Technology Center at Texas A&M University. Homopolar welding is being readied for commercial use.

**WAXING OPTIMISTIC.** Oil companies are putting big bucks into one of the stickiest problems that drove them out of subsea production two decades ago—namely, clogging. As crude oil cools in the 40-degree waters of the ocean floor, paraffins from the waxy Gulf oil form on the inside of pipelines. Today, insulated or water-heated pipes keep oil from cooling and precipitating wax. Some companies inject chemicals that heat on contact, dissolving the waxes. But both methods can be costly and they don't always work.

A cheap new anticlogging method that doesn't require costly pipe or regular chemical injections may be on the way. Working with the National High Magnetic Field Laboratory at Florida State University in Tallahassee, oil companies are trying to determine whether magnets attached to subsea pipes will keep paraffin in crude oil from clumping. There is some evidence, says Laboratory Director Jack Crow, that iron particles contained in crude are binding with the wax, preventing larger clumps from occurring.

The magnet study is just getting underway, and many other obstacles to deepwater production remain. Some companies have shied away from subsea programs. For instance, Oryx Energy Co. is planning instead to use a new type of tethered, floating platform called a SPAR, saving the cost of building steel skeletons thousands of feet deep. But lots of other companies are counting on ocean-floor production when there's a mile or so of salt water between them and a fortune in oil and gas.

By Gary McWilliams in Houston



## Your Business Is Growing. Congratulations. Who's Going To Do All The Work?

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# The Corporation

be. In fact, the 42-year-old chief acknowledges he is still feeling his way. "I think we do have a better sense of where we want to go," he says. "But how we get there and what has to be done to get there are issues that we wrestle with every day."

Focusing this chaotic marketer is Farah's No. 1 problem. In his defense, he wasn't given much to work with. The retailer has a grab bag of specialty businesses that sell everything from shoes to furniture to costume jewelry (table). The only clear winner is Foot Locker, a shoe chain that is running into a lot more competition.

Building a core business around Foot Locker and dumping much of the rest seems like an obvious step. But Farah says it's not that easy to pare—many outfits were in far worse shape than he expected. "We made a decision that we're going to have to improve almost all of the businesses before we can begin to make more serious portfolio decisions," says Farah, adding that he expects that improvement to take at least another year. "Just to dump things at this point and take a loss is not in the cards."

Not everyone applauds that strategy. "The company is famous for patience that borders on the insipid," says retail consultant Alan G. Millstein. "Shareholders and Wall Street would like someone more decisive in getting rid of some of the limbs that are unprofitable."

**WHAT SELLS.** Farah, who earned an MBA from the Wharton School, has plenty of experience figuring out what will sell in stores, but little in turning around troubled companies. He got his start at Saks Fifth Avenue, where he was an early advocate of European designers for men. He then went on to Federated Department Stores, where he helped expand Rich's, the Atlanta-based chain, eventually rising to head of merchandising at Federated. His three-month stint running R. H. Macy & Co. was cut short when the company was acquired by Federated. To help him in his new role, Farah has recruited heavily from the outside. President Dale W. Hilpert,

for example, was lured from Payless ShoeSource Inc. in April.

The problems at Woolworth extend beyond just meshing the company's flailing assets. Woolworth lags way behind rivals on such matters as information systems, productivity, and controlling expenses. Weak inventory control, for instance, forced Farah to liquidate \$100 million in old merchan-

dise and take a \$38 million inventory write-down. But finding the money to fix those problems could be tough. By the end of last year—about the time Farah took the helm—Woolworth's debt had climbed to 71% of total capital, up from 46% in 1990. To help trim borrowings, Farah cut capital expenditures by 25%, to \$163 million.

Farah has made cleaning up the balance sheet his top priority. And with good reason. In the first quarter of this year, all three major rating agencies downgraded Woolworth's debt to low-investment grade. In April, Farah eliminated Woolworth's dividend, a savings

of \$80 million a year. He lopped a further \$100 million off the annual budget by cutting 2,000 jobs. Most of the savings have gone to reduce short-term debt, which had ballooned to \$1.3 billion by the middle of 1994. "They're out of Caldor country," said one investor, referring to the regional discounter that recently filed for Chapter 11.

Farah has dedicated \$30 million to the shrunken capital budget to bringing Woolworth's namesake variety stores started in 1879, into the computer age. The stores were perennially out of stock on popular items, while other products rotted on the shelves. But that's only part of the problem. The Woolworth stores are stale, dingy, and cluttered. Farah plans major renovations. But the business doesn't pick up, and doesn't rule out selling the namesake stores.

Meanwhile, he's relying on two specialty-store concepts—Foot Locker and Northern Reflections—to fuel growth through the transition. Both are problematic. Relying on Foot Locker is no surprise. With sales of \$3.5 billion, the athletic-footwear and apparel division, which includes Foot Locker for kids and women, is by far Woolworth's largest.

Foot Locker fueled much of Woolworth's growth in the 1980s, but the concept is growing old, and competition stiffer. Operating profits for the division are almost 40% below 1992 levels.

Farah is also betting on Northern Reflections, a little-known Canadian chain

that has migrated south. The Northern group, which includes spin-offs for men and children, has 662 stores and is growing fast. Stores open for more than a year have shown healthy gains, but the chain is dwarfed by market leaders such as Eddie Bauer and Lands' End. The division, which also includes a handful of other specialty retailers, generates only \$656 million in sales—not enough to have a major impact on the billion company. Foot Locker and Northern Reflections may let Woolworth limp through a transition. The question is a transition to what?

*By Lori Bongiorno in New York*

## THESE PIECES DON'T FIT

CEO Roger Farah has more than 40 unrelated chains to puzzle through. Among them:







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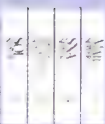
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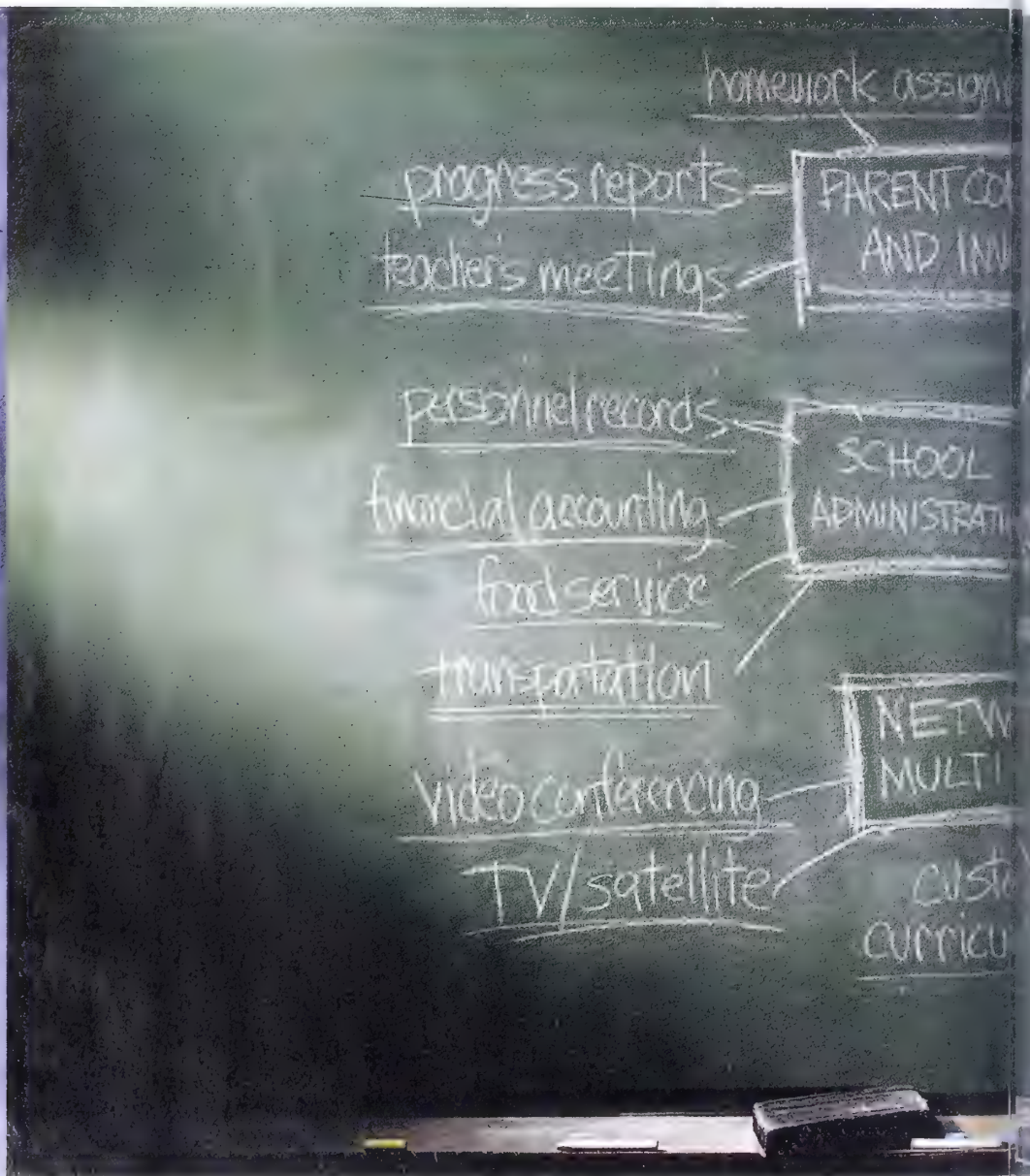
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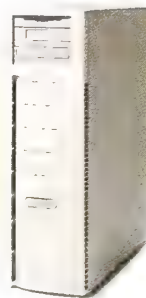
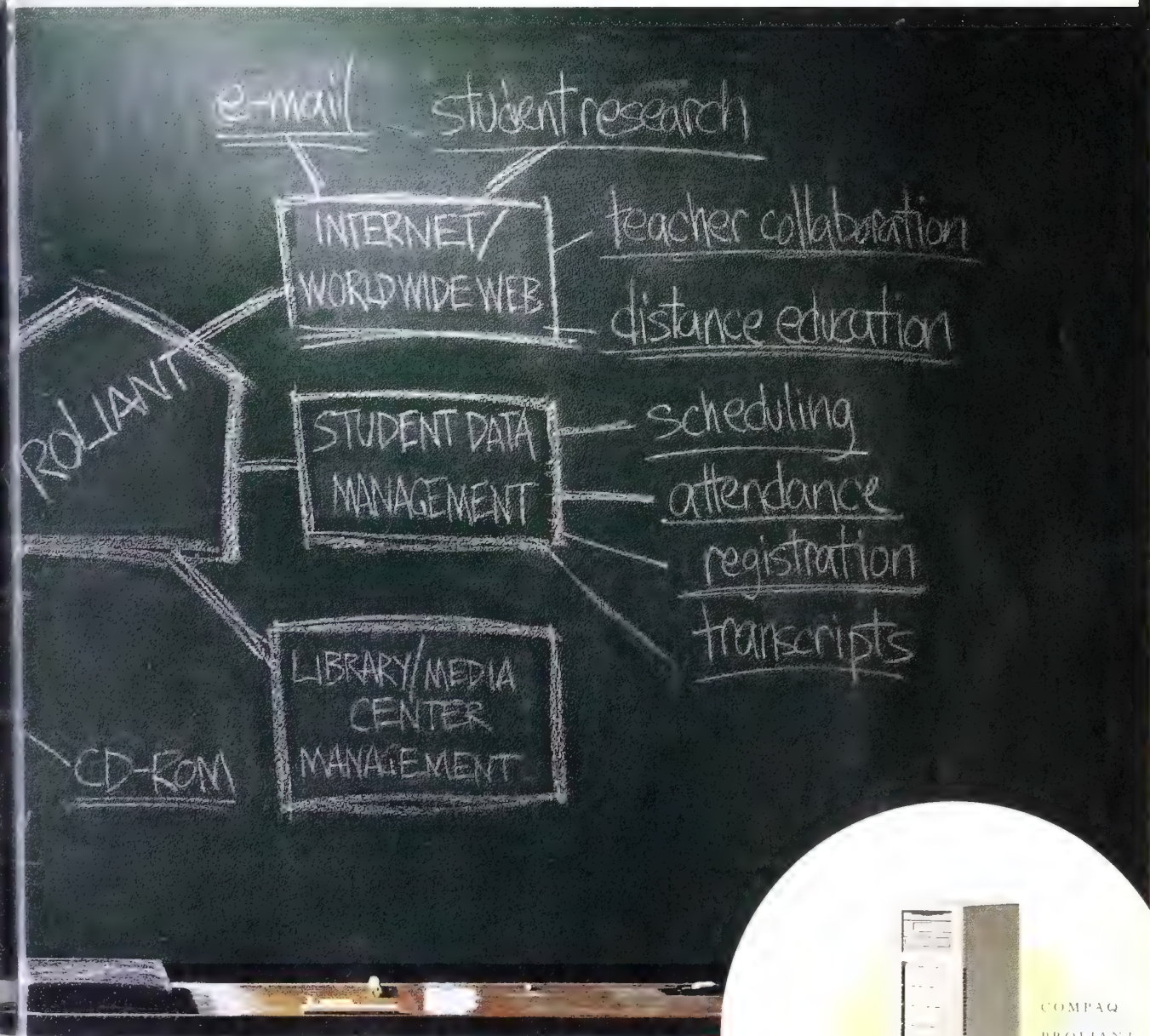
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# At Last

the American educational system, the part of it where schools and companies intersect, is in a can-do phase. And it's called quite simply school-to-work.

Instead of focusing so much on financial support to improve America's schools, companies from BellSouth, Compaq, and IBM to General Motors, Matsushita, and UNUM are rolling up their sleeves and directly participating in a major campaign to help students fit better into the emerging workplace of the 21st century.

"It's on everybody's agenda — the Business Roundtable, the U. S. Chamber of Commerce, the Conference Board, the National Alliance of Business, and many trade associations," says Bob Soltys, executive director of the new National Employer Leadership Council, whose founding members include a cross section of industry from American Express and Cybernet Systems to Thom McAn, Peavey Electronics, and Siemens. "We call it school-to-career. 'Work' has a manual-labor flavor to it."

**Win-win Scenario.** These days companies have little choice except to jump in and do something. Out of sheer self-interest — the desperate need to find 'winners' among graduating classes — companies are no longer acting

like spectators but are beginning to play a very active role in shaping education. How can they do otherwise — with jobs becoming more complex and high-tech day by day?

In a kind of win-win negotiation — with secondary schools, community colleges, and institutions higher up the ladder — companies are proving that it's also to the advantage of schools and their students to design programs that are in tune with the realities of today's and tomorrow's workplace.

**Information Workers.** "Companies are deconstructing and constructing as never before," says Hilary Pennington, president of Jobs for the Future, which has served as a matchmaker between schools and industry for more than a decade. "The nature of jobs is radically changing. There's a new premium on soft skills. What we're seeing is that different occupations are becoming more similar. The new factor is the manipulation of information — whether in manufacturing, an insurance company, or an oil refinery."

Beyond that, it's a new kind of confident, empowered "information worker" who is becoming the role model. In ideal form, the versatile toiler of the future will communicate effectively, solve problems swiftly and creatively, concentrate on quality, and — as Pennington

(continued on page 1)

## SUCCESS AT SIEMENS:

*Young employees develop toolmaking skills at Siemens Electromechanical Components' training center in Franklin, Kentucky. Patterned after the German model, the company's 30-month apprenticeship program combines classroom education with hands-on experience under the supervision of master technicians.*



The text of "Will We Win?" was written by Paul Burnham Finney, a former Managing Editor of *Business Week* magazine and a writer on business and educational topics.



## Education Secretary Richard W. Riley

### How the Non-Traditional Becomes Traditional

**A**s two-term governor of South Carolina, Richard W. Riley revamped the state's school system. Now, as Secretary of Education, he has quietly pushed various reforms on a national scale — among them, Goals 2000, which helps define core subjects American students should master, and the School-to-Work Opportunities Act, which he helped shepherd through Congress with Labor Secretary Robert B. Reich.

#### Why is there such excitement now about school-to-work programs?

The needs of the workplace have changed so dramatically that there's little long-term value in having an employee who can only do a specific task and do it well. Job requirements are moving and churning and turning and changing, and what's most important happens to be knowledge of core subjects so that young people can quickly learn new skills.

#### What are the core subjects?

Goals 2000 names the core subjects, which we recommend for the states to include in their curriculum. It lists with academic standards. You of course have English, math, and science. You always start with reading ability — any job. Also writing. You get into history and geography. And economics is very important.

#### Q. How do you set benchmarks or standards?

**A.** When we use the term "standards," we're referring to what a student should know and be able to do in a subject at a particular grade level — say, what an eighth grader should know about science. It's a support system for the states. Most states have used Goals 2000 to help define what's a good education.

#### Information Superhighway

##### Q. Where does the information superhighway play a role?

**A.** The superhighway has to fit into the modern classroom. There's a very important direction education is now taking: the use of technology in the process of educating people. It's important for teachers to learn how to reach students with and through this technology. You have to have software available — for young people to learn this technology.

##### Q. Doesn't the rearrangement of curricula to accommodate new technology rub traditionalists the wrong way?

**A.** Those folks are very few in number and diminishing rapidly. While all teachers and administrators could use a lot more training to understand computers and technology better, most, in all fairness, are aware of the importance of this aspect of learning. You're seeing schools everywhere trying to get more computers and expand teaching capacity of the computer field.

##### Q. Any particular types of schools you're thinking of?

**A.** Those in vocational areas. We used to teach general math. And we

graduated students who could provide a specific service. That's totally inadequate now.

##### Q. Aren't these new requirements too tough on the disadvantaged?

**A.** The idea of drifting through school and dumbing down education is a thing of the past. That's particularly true for the disadvantaged. For years they got watered-down curriculums. But we've shifted out of all of that now with the Title I program. A lot of young people in high school end up going into school-to-work programs.

##### Q. Where do you place school-to-work programs in the whole scheme of American education?

**A.** I classify it as the total restructuring of the American high school.

The idea is that education can't just take place in the classroom. It has to be relevant to what employers want young people to learn.

##### Q. Hasn't secondary education been on a double track — for the work-bound and the college-bound?

**A.** When you look at how high schools have functioned, you see

this separation of young people who are going to college and those who aren't. The latter are on the general track. They often end up in vocational schools and similar areas of education.

##### Q. So, where's the restructuring?

**A.** The whole concept of high school has changed. In-school work is challenging all students. It used to be you could get by with less. Now all students have the same standards. That's a radical difference.



Education Secretary Riley: 'In-school work is challenging all students.'



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**Q. Is the old distinction between blue-collar and white-collar jobs obsolete?**

**A.** Blue and white are disappearing. The whole school-to-work process is designed to do that.

**Q. In what way?**

**A.** Young people who go into a school-to-work program learn in a different way. They're directly preparing for careers. It's hands-on learning that's more relevant to their lives. And they're developing skills in areas they're interested in and have chosen. In a bank, a hospital, a plant. And it's partly in anticipation of going to college.

**Q. Community colleges?**

**A.** I don't think anyone realizes how important community colleges are to this country. They developed because of the vast need for them. They've gotten better and better.

**Q. What about the role of companies?**

**A.** Enlightened companies that are concerned with progress and improvement are very much into the school-to-work idea of getting workers who are qualified and high producers. They understand it. It's very practical — not just something you read in a magazine.

**Q. Could you call it simply good teamwork?**

**A.** Yes, it's a coming together. It's cooperation and partnering. That's what it's all about. And that's why it's powerful. You get students together with parents and teachers and employers.

**Q. Should all companies jump on the school-to-work bandwagon?**

**A.** Not necessarily. It comes down to local decision-making. Every company has different requirements, different processes, different cohorts of students to deal with.

**Q. What's the federal government's role in all this?**



**MEETING OF THE MINDS:** Secretary of Labor Reich, Secretary of Education Riley, and Jamie Houghton, chairman and chief executive officer of Corning Inc. and chairman of the National Skill Standards Board.

**A.** It's not for Washington to solve all these problems. We prefer for the federal government to support state and local efforts and to act as a clearinghouse for good ideas and information. For example, Seattle's experiment might be tried out in Louisville. We don't take the approach, here's the shoe and force your foot into it.

**Q. Has the School-to-Work Act had the impact you expected?**

**A.** The people involved are very pleased. We've gotten good indications. A first group of eight states are implementing it. Probably within the next few weeks we'll announce 20 more states.

**Q. Is the new Skill Standards Board working well?**

**A.** It's very helpful in taking a career and defining it. Not just little fine-line definitions of a skill. It shouldn't be that. You learn through a job to reach those skill standards. At the same time, you're learning academic subjects within the Goals 2000 framework. The two complement each other.

**Q. In all this, what happens to the American dream of giving your kids a college education?**

**A.** The way things are done now, the nontraditional has become traditional. It's a wonderful change that has come

about. I was speaking to a graduating class in Dade County a couple of years ago — a diverse body of students at a community college. The percentage of graduates who were going to go for a four-year degree was amazing. They saw themselves as improving.

**Q. So, you'd say that the best school-to-work projects build higher education into their programs?**

**A.** Yes, students now can follow a nontraditional path to a degree. It's interesting that in a recent poll some 96% — or 97% — of parents said they'd like to send their children to college. This is the Education Era in the history of civilization — the time when education is the most important thing in our economy and our future. It's good that American parents want their children to have experience beyond high school. We have the best higher education system in the world. Students all over the world are trying to get into our schools.

**Q. But not all students have the means and connections to go on to college.**

**A.** The big job — and Bob Reich and I talk about this frequently — is to make sure that young people have access to higher education. The hard thing is the preparation, the timing, the tuition.

**Q. Can't companies be of great help?**

**A.** Yes, in school-to-work programs they can make work and education schedules fit together — for instance, late afternoon or night classes at a community college.

**Q. In your prescription, education seems to go on and on.**

**A.** Education breeds more education. We talk now about life-long learning. Every person, whether it's someone in a school-to-work program or an older employee, has to understand that education doesn't stop at high school or even at the college level.

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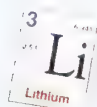
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says — “manage change.” And make decisions at lower levels of the corporate hierarchy without getting their boss — or other higher-ups — angry?

To some extent, the excitement generated by school-to-work programs comes out of frustration with the pace of change in the American education system. The ongoing “crisis in American education” seems a bit stale as new numbers surface that show that students are scoring well on tests in many areas — SATs in particular. In the global sweepstakes, where education has become a matter of national rivalry, countries with supposedly estimable schools such as Japan have turned out to be vulnerable in key respects — for instance, social adaptation. And here at home, there’s hardly a great new idea about how to reform schools; from “virtual schools” linked by computers to old-fashioned classrooms supervised by disen-

chanted parents, that hasn’t been presented, aired, debated, and chewed over in endless seminars and, in some cases, implemented.

**Renaissance.** That’s largely why the old and simple idea — training kids for a real job in the real world — is going through a renaissance.

Spurring the adjustment to change is the emergence of a global marketplace where goods, services, and investments freely flow across national boundaries and corporate competitiveness has a take-no-prisoners kind of determination. In this battleground, there’s little room for the less motivated worker — the one who just gets by.

“The reason school-to-work is so hot, if you will, is that it encompasses a lot of ideas that have been floating around,” says JD Hoyer,

director of the national school-to-work office in the Department of Labor. “School-to-work provides a framework for an education that will lead to something. After all, education must provide more than continuous learning. ‘Is my child going to be okay financially?’ It’s worry of people.”

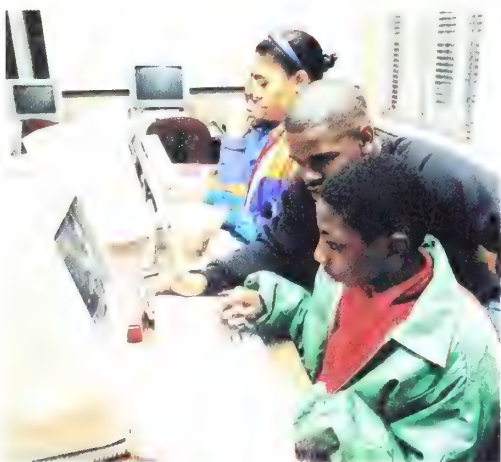
## A Program That’s a Process

In any case, school-to-work is a slightly awkward label that describes a process rather than a program — a transition from a classroom setting to a corporate environment.

**The Dignity of Work.** Since 1994, the School-to-Work Opportunities Act, which commanded bipartisan support, has helped smooth the shift from studying to working. In the wake of its enactment, top corporate leaders met with President Clinton last December and “hit the ground running at the beginning of this year,” as Soltys puts it, with the formation of the National Economic Leadership Council. It’s spearheading a drive to help companies develop well-structured school-to-work programs tailored to corporate, school, and community needs.



**IBM'S IDEA:** Make computers a natural part of the hands-on classroom experience so that students can learn by doing.



**AETNA ACADEMIES:** Students expand their critical thinking and problem solving skills through hands-on activities and projects at the insurance company's Saturday Academies.



**Lincoln always believed the word was  
mightier than the sword.**

In 1858, Abraham Lincoln debated Stephen Douglas on the social issues of the time. In 1995, nearly 20,000 high school students will argue significant moral and value issues facing our society in the Lincoln Life Lincoln-Douglas Debates, sponsored jointly with the National Forensic League.

Our sponsorship underscores our dedication to the preservation of President Lincoln's legacy of truth, straight talk, and personal conviction. By participating in the debates, students arm themselves with the power of words to resolve differences, tackle tough issues, and build character.

To learn more about the Lincoln Life Lincoln-Douglas Debates, write the National Forensic League, P.O. Box 38, Ripon, WI 54971, or call (414) 748-6206.





**CERTIFIED SKILLS:**

*Anika Thorbourne, a high school student in Virginia Beach, scored 40 points above the national average on the Novell national certification exam. She took the high-tech high school training program sponsored by Compaq, Electronic Systems, Novell, and the Virginia Beach City Public Schools.*

At its best, school-to-work is the tunnel of education with a light at the end — a job that pays, whether you're a worker in a steel mill, a programmer in a database-management company, or an assistant to the assistant curator in a museum. In short, you have a known destination to which you're heading, diploma or certificate in hand.

**Awake in Class.** Let students get a taste of what's ahead — in a career, as an adult, in the big, wide world — and suddenly there's a reason to stay awake in class. You might even make some money if you do, young people have discovered.

"There are a lot of kids in school with hats on backward who ask, 'Do I stay here all day?'" says Soltys, a former IBMer. "They don't have a clue as to what the work ethic is all about. They not only must have academic smarts but also practical abilities. All too often, they don't know how to apply the theoretical to the practical."

Making that connection has been the driving

force behind the National Academy Foundation. Since its founding a decade ago largely under the aegis of American Express, it has helped create schools-within-schools across the nation. "The two-year experience at these academies has changed the lives of kids who never thought of going to college," says Charlotte K. Frank, one of The McGraw-Hill Companies' school publishing executives and savvy observer of developments in education, adding admiringly, "It's just a wonderful opportunity. It prepares students for the real world of finance, insurance, real estate, tourism, and public service."

**Flexible Format.** When a school-to-work program is good, it can be very, very good, enabling students not only to establish clear goals but to keep developing skills in a very flexible mode.

That can mean learning about business in the classroom, working directly in a company as an apprentice or intern, detouring to take

courses at a community college, returning to the workplace, and then — even after all that — choosing to complete four years of college. It's an educational path with zigs and zags that combines traditional learning with personal achievement through customized schooling. It bears little resemblance to the school with four walls. This one has five, six, or more sides to it.

Today's classrooms can even include instruction on the import of the World War II holocaust. Through videotape, books, and other materials the new United States Holocaust Memorial Museum in Washington, D.C. helps schools send a strong message to students about the need for eliminating indifference, racism, and intolerance in contemporary society.

## Technology Turmoil

**M**ore than anything, the flashy decade of the '80s masked the essential problem: how to find jobs for the nation's graduates. Everything in the economy seemed to flow in such rich abundance that you could overlook the imbalance



## PARACHUTES NEEDED!

Making the plunge to the real world can be tough going for students. SIFE, or Students In Free Enterprise, is a not-for-profit organization whose singular mission is to work in partnership with higher education and business to provide college students the leadership experience of teaching others how market economies and businesses operate, and how to use this knowledge to better themselves, their communities, and their countries. For more information, please write to: Students In Free Enterprise, The Jack Shewmaker Center, 1959 East Kerr, Springfield, Missouri 65803. Or call us toll-free at 1-800-677-SIFE.



between young people and available jobs.

**Eye-Openers.** Yet there were plenty of warning signs that students emerging from high school or college were about to enter a hostile job environment in which their classroom talents might not have much relevance. If nothing else, the arrival of the ill-defined and imposing information superhighway threw the workplace into turmoil. Would there be an information — call it computer — component in every important job out there?

Talk about a downer for the nation's kids, let alone schools. Both educators and employers agree that a surprising number of teenagers now sense — even fear — that what happens in school has little bearing on what will take place in adult life. And this instantly translates into a lack of motivation — a sense of boredom — in which the dazzle of movies, television, arcade games, and other diversions makes the earnest study of math and biology seem dull.

Real-time apprenticeships or internships — at a fast-food store, TV station, retail outlet, or nearby factory — can be an eye-opener. From Junior Achievement's creation of classroom companies to the Students In Free Enterprise's (SIFE) effort to train students to think entrepreneurially, the exposure to life in the workplace has a telling and positive effect in turning on young people.

**Problem Solvers.** Why has there been such a gap between study and work?

"The problem is that schools and industries weren't communicating," says Margot Brown of Motorola. But it runs deeper than that.

Even when the two were on speaking terms, the corporate side of the equation was in a



**MATSUSHITA MAGIC:** A Panasonic employee volunteer assists students participating in "Kid Witness News," a hands-on video education program now making waves in some 200 schools across the U.S.

state of turmoil — a condition that continues to this day and will go on into the future. There's no denying that with companies downsizing, reengineering, and restructuring, few top managements are entirely sure of what they want each and every job applicant to do.

How can they be certain — with markets going global, new technology coming on stream at lightning speed, and the drumfire of information on TV and over the Internet constantly changing the public's likes and dislikes?

So it's understandable that in a generic sense, many employers are looking for entry-level applicants who fit a job description that reads: "Required: a problem solver with various high-tech skills who can communicate and work in a team."

## Back To Adam Smith

**P**robably the signal appeal of an effective school-to-work program is the way it delivers on its promise. Rather than an abstraction — such as "let's develop the minds

new top manage-  
ments are entirely  
re of what they  
want each and  
every job applicant  
do. How can  
they with markets  
going global and  
new technology  
coming on  
stream?"



**O'S AIM:** Supporting LARN (Los Angeles Education Alliance for Restructuring Now) and programs designed to bring schools and the workplace closer together.





Panasonic

# One of the largest teams at the Olympic Games does not run, swim or jump.

While this team may not be particularly athletic, its training requires the same precision, dedication and grueling regimen of an Olympic athlete. It is the team of Matsushita engineers and technicians committed to help broadcast more than 3,000 hours of Olympic events to the world.

But our role at the Olympic Games goes far beyond technological support. As Official Broadcast Equipment and System Supplier, Matsushita Electric has joined with Clark Atlanta University and Atlanta Olympic Broadcasting to create an innovative program. Using the same Panasonic digital video equipment that will capture the drama of the Olympic Games, some 1200 students are training in the hopes of becoming part of the



broadcast team for the  
Olympic Games.

This innovative program is just one example of what Matsushita means when we say, "We're more than a sponsor, we're part of the team."

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**Matsushita Electric**  
Panasonic Technics *Quasar*

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of our young people" — it's a show-and-tell approach to which Americans are enormously and viscerally attracted. And it is a formulation that fits with the drastically reorchestrated structure of American society as it moves — or stumbles — into the 21st century.

Today, there's a much friendlier attitude on the part of students toward companies — and how they go about making money — than there was in the '60s and '70s. This grows out of the awareness that there's an economic aspect to almost everything that occurs in

**'The automaker traces the improved relations between employers and educators partly to the drive for quality that began with the Malcolm Baldrige Awards.'**

## Case In Point

### What Ford Found Out About the Workplace

**W**e're getting away from the idea of repetitive factory work," says Marcus Clarke, manager of external and governmental education and training at Ford, which supports the Ford Academy of Manufacturing Sciences (FAMS). "We want to encourage students to go on to higher education — a two-year school and beyond — if they choose to do so. Everything we do in society now has a technical component. You can't operate a

■ Every worker has to have some technical literacy.

How do you take these basics down to the high school level? Here's how Clarke sees it:

■ Students need more hands-on experience with math and science. Example: a science project that integrates academic study with experience in, say, a Ford plant.

■ There must be an ongoing link between what you learn in school and what you'll do in a career. "How does school work fit into the real world?" asks Clarke. "That's the definition of school-to-work."

■ Teachers need reorientation so that they run classrooms the interactive way. "Take a biology teacher," explains Clarke. "We'd say biology is basic for learning about the human anatomy, and that can lead to an understanding of the ecology of our vehicles — how humans act or interact with cars."

#### Global Perspective

In the FAMS program, a variety of things merge work and study. It gives teachers an opportunity to spend time in industry to see what work is really like and how high school courses can relate to it. And students mix summer work with classroom studies, with encouragement to "help

others" and "to go back and learn more if they want to."

FAMS is only a somewhat distant cousin of the apprenticeship program developed by Siemens. "We follow an academic model with roots in the United States — it's designed for our way of learning and our culture," says Clarke. "The Siemens model has distinctly German characteristics. Germany has always made math and science a part of its culture. The Siemens apprenticeship program seems very focused. It's to train technicians to build and service the products they manufacture."

More than most companies, Ford is very sensitive to the impact of global operations on its employment structure. "Our standard of living — our benchmark — is to keep competing globally," says Clarke. "You don't compete as much in services as you do in manufacturing — services usually require adaptation to very different national and local conditions."

Ford believes that the uneasy relationship between employers and educators has improved. It traces the change partly to the drive for quality that began with the Malcolm Baldrige Awards.

Says Clarke, "You have to turn on the lights in the heads of the high school students."



**FAMS IN FOCUS:** Ford's goal is to train students at its Ford Academy of Manufacturing Sciences (FAMS) so they are technically literate and team players in the global workplace.

VCR or microwave — certainly our cars as well — without the processing capabilities that didn't exist not long ago. They all now have microchips."

Clarke did a major study for Ford Motor — a "future scan," as he calls it — to help better define job requirements. The project took him around the U. S. and overseas to Germany and Japan.

Here's what he concluded:

■ Turning out a good product depends on teamwork.



**TOYOTA TRAINING:** Students at Automotive High School in Brooklyn learn engineering skills through the Toyota Technical Education Network. The maker has T-Ten programs up and running in 10 schools in 40 states.

society, even including the merchandising of art and culture.

Ironically, the decline of hostility between educators and employers — or students and companies — comes at a time when corporations are no longer security blankets, ensuring

cradle-to-grave employment once you're on the payroll. Now there's a kind of unspoken truce in which students have an understanding of corporate nimbleness, if not fickleness, and companies defensively — or out of guilt — try to train and develop well-rounded employees.

**Packaging the Product.** The fact that school-to-work is a hot trend ultimately comes down to Adam Smith's laws of supply and demand. In a 1990's formulation, subscribed to by educators and employers alike, schools provide a "product" — educated students — while companies constitute the marketplace for their skills and talents. If the two are out of sync, it's not much different from the case of a company putting a product on the market and seeing it bomb because consumers don't like or need it.

So, harsh as it may sound, school-to-work

programs are only as good as the guidance they get from both educators and employers. That involvement is essential to make sure the education establishment is producing the kind of graduates that companies find desirable.

"I see a large role for employers in school-to-work programs," says John L. Glendenin, chairman of BellSouth. "We need to be an integral part of a system that keeps curricula in tune with the workplace and eases the move of young people from school to jobs. Employers and educators have to work together to create the kind of educated workforce that can carry the nation into the Information Age."

### Skills That Siemens Hones

**A**lbert Hoser, president and chief executive officer of U.S. operations for Siemens, the German electrical and electronics giant, is a big fan of the Siemens Apprenticeship Program. Guess why? That's where he began his career. And now the program, modeled after the German concept of getting employers, educators, union bosses, and community leaders together, is one of the most admired school-to-work systems in the U.S.

Siemens has gone about combining academic excellence with hands-on factory work. Former principal of a top New York City public high school, John Tobin masterminds Siemens' outstanding program. Here's his take on it:

"We embrace the empowered-worker

**JOBS FOR THE FUTURE:** Valentino Rivas, who now works at Brigham and Women's Hospital in Boston, graduated from English High School where he was a Pre-AP student. The program is part of the Boston School-to-Career System supported by the city's public schools and the Boston Private Industry Council. Boston is one of five cities that are part of Jobs for the Future's Benchmark Communities Initiative.







'Mrs. Alvarez, how



"They've asked me how  
to feed the guinea pig.

"They've asked me how  
to draw a dinosaur.

But today a student  
asked me.

## Do I telnet into a remote server?" "

To teach our kids  
the skills they need, our  
teachers have to learn  
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part of 'Reinventing  
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We're providing fund-  
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helping to develop schools  
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Because when our  
teachers can get the most  
out of technology, so will  
our kids.



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concept, but put it in the context of skill sets in manufacturing.

"We're looking for workers with very broad skills, certainly in terms of teamwork, understanding the broad organization, grasping the details of manufacturing from the bottom all the way up to customer service. But it's also very important for our people to have some hands-on skills that they can perform to a standard."

**Worthless Certificates.** "What led us to all this?" says Tobin. "Well, supply and demand have been out of sync. In some markets we just can't find employees."

"For example, in the heart of Kentucky, Siemens was unable to get precision toolmakers. We were recruiting them from Germany and Switzerland. Then we tried hiring Americans who seemed to have certain skills on paper — but their certificates didn't turn out to mean anything."

#### NBEA IN ACTION:

*Tony Award winner Matthew Broderick, starring on Broadway in "How to Succeed in Business Without Really Trying," is showing kids how to succeed in the real world by promoting attention-getting business courses sponsored by the National Business Education Association.*



**COLLEGE-BOUND AT GE:** A big-impact program largely for inner-city and poor schools in some dozen cities from Cincinnati to Durham. Overseeing it is General Electric executive vice-president Frank P. Doyle, who doubles as chairman of the board of Jobs for the Future.

"We're not just transplanting the German school-to-work system," he says. "We've adapted it to American conditions. We use some of its best practices. Our apprentices, for example, take a mid-term and final exam in electrical communication technology and precision toolmaking. And we always make our programs a steppingstone to a university degree."

"You can't sell American parents and kids on the idea of entering a skilled-work program without the opportunity of getting a university degree — not after the democratization of education 50 years ago with the G.I. bill. They may not go to the university level, but they have to have that option."

"Siemens has a boiler-room through boardroom philosophy that says that the issues that impact on our business affect all levels of the work force," says Tobin. "That includes management education. In our apprenticeship and other training programs the participants rotate through all the jobs on the floor. That gives them a good logistical picture — from production to support services. And they can go to a university and come back to us. That's a much better engineer than one with just theoretical talent."

"Albert Hosen himself demonstrates that apprenticeship isn't a dead-end position. It's very upwardly mobile. You can move through the organization to the highest level."

**Factory Floor.** "Teachers teach kids to live in a world they don't really live in," says Tobin going to the bottom line. "It's academic. It's simulated. So we've hired teachers to corral work for us during the summer so they'll

**MATTHEW BRODERICK STARS IN THE BROADWAY HIT**

**I WANT YOU TO SUCCEED!**

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**ARE YOU READY FOR YOUR FUTURE ABOVE AVERAGE, COLLEGE OR UNIVERSITY?**

**TAKE CARE OF YOURSELF. TAKE BUSINESS EDUCATION.**

## Labor Secretary Robert B. Reich

### How To Shape Education to Fit the Workplace

**S**ince becoming Secretary of Labor, Robert B. Reich has been on the road as much as in the office, observing the interface between education and work in dozens of communities. Here are his thoughts.

**Q. Is there a mismatch between education and jobs?**

**A.** It's not a good fit. We have one of the best systems of higher education but one of the worst for getting young people from school to work.

**Q. What's wrong with K-12 education these days?**

**A.** All too often our schools replicate the production system developed during the industrial revolution. People move through school just like product on an assembly line. We treat students the way we do a machine-made product. Periodically, we take samples to see whether there are any errors or mistakes. And if the product doesn't have everything you want, it goes back to an earlier point in the assembly line. Doesn't that sound like a lot of today's schooling?

**Q. Why is the school-to-work movement so popular these days?**

**A.** It's taken off because it works. Again and again, as I travel around the country, young people who are in danger of dropping out — or are simply bored — describe to me in glowing terms how much they're learning in these programs.

**Q. Are school-to-work programs the magic answer?**

**A.** Let's not ask too much of these programs. We're dealing with eleventh and twelfth graders. We want to enrich classrooms, open the eyes of the young to a world where fewer and fewer jobs involve routine work.

**Q. On a reality check, just what should school-to-work programs do?**

**A.** They're not going to get at all the skills you need. The most important goal is learning how to learn. Identifying how to get information. Learning how to assimilate new knowledge. Figuring out central problems.

**Q. When you say that, are you thinking of the global marketplace?**

**A.** No, not necessarily a highfalutin multinational situation. The challenge to a worker may be in a mundane part of the American service economy. I've seen retail workers who understand the complexities of the merchandise they're selling and help guide consumers. Why, some of the salespeople at Home Depot act like consultants, interviewing customers to determine their exact needs and then making recommendations.

**Q. What's the advantage of a college education today?**

**A.** Your chances of landing a good job are higher. A bachelor's degree provides a kind of Good Housekeeping Seal of Approval. It's an assurance that this person has mastered certain minimal communications and math skills. By attending college, students also make a lot of contacts.



**LABOR SECRETARY REICH:**  
*'The most important goal is learning how to learn.'*

### Zigzag Career Paths

**Q. Is there a straight route between school and work?**

**A.** No. Some students move into a job, then go back to school, then get corporate training — and then after working they might even decide to go the full route through a two-year or four-year college. The road has more choices, more detours.

**Q. Is school-to-work just vocational education with a new label?**

**A.** It removes the old barrier between academic and vocational education. Ultimately, this kind of learning is for all young people. When it's working right, the school and job are integrated — the mentor knows

what the teacher is teaching.

**Q. And the kids are more motivated?**

**A.** In New York City I met a bunch of students in a high school in West Harlem — mostly African-American and Dominican kids. They were working with a phone company — I think it was Nynex — and a hospital. And what they were learning in the classroom began to come alive on the job. They saw how biology had a bearing on a job as a health technician.

**Q. Is school-to-work useful mostly for encouraging inner-city kids?**

**A.** It's not just for disadvantaged students. I'm convinced it works for almost everybody.

**Q. Doesn't the new emphasis on skills training inhibit the development of creative minds?**



"I believe these kids  
Now I've got to



You'd think getting a bunch of teenagers to study engineering in their free time would be impossible. But Al Ware, of General Motors' Vehicle Launch Center, helped get 5,000 students enrolled in the Detroit Area Pre-College Engineering Program this year. They take advanced science and math courses. They do engineering projects like building



ill make great engineers.  
ake them believe it."



General Motors.

ll-scale moveable car entirely from paper. And they learn they can solve just  
ut any problem they set their minds to solve. Al says, "The more we put into  
community, the more we'll get out of it." He's right. Because some former teen-  
s he inspired are designing better automobiles at GM today.





**A.** We can get geniuses out of a school-to-work system. As I've observed around the country, many extremely bright students find their studies enlivened — and made much richer and more exciting — by seeing real world applications.

### Knowledge Workers

**Q. Who's this knowledge worker you've written and spoken about?**

**A.** The nature of work these days is such that you have to identify and solve complex problems. More and more, you have to work with symbols — math symbols, software icons, language symbols. The modern worker has to rearrange symbols to find the solutions to problems.

**Q. Would you bring that down to earth?**

**A.** Even cashiers on checkout lines have a computer to provide a database and tell them what to reorder. They become inventory managers. There's some judgment required.

**Q. Doesn't technology make many jobs obsolete?**

**A.** It can either reduce or expand work. In some cases, technology has eliminated jobs. But I've also seen technology enhance the jobs of workers who hold down fairly menial positions. They have more choices, more decision-making.

**Q. If there's more empowerment, how does an independent-minded worker get along on a team?**

**A.** The ability to work constructively with others will be one of the most important qualities of jobs in the 21st century. The lone inventor or entrepreneur is increasingly a thing of the past. Any product you look at is a consequence of a group of people sharing their knowledge and insights. Even the assembly line is giving way to teams.

**Q. Are bright individuals too competitive to be cooperative?**

**A.** Scientists — to take one example — work in teams and have brainstorming sessions. Today no single person has all the knowledge, all the answers.

**Q. Don't you have to be a quick study to be successful in this new work environment?**

**A.** Yes. Over the past 50 years there's been a shift in demand in favor of workers who can learn quickly on the



**BRIGHTER FUTURE:** Jonathan Boggs, who has taken electronics in the High Schools That Work program, can smile about the skills he has learned and a career that lies ahead.

job — and against those who are learning how to learn. A large portion of the work force is simply unprepared to continuously learn on the job. And their wages have been declining.

### Gold-Collar Winners

**Q. Is the two-tier work force — blue vs. white collar — disappearing?**

**A.** It's neither blue collar nor white collar. Now you have gold collars and — well — frayed collars. You're a top professional, someone who's doing better and better, or a frayed-collar worker who doesn't have the learning skills.

**Q. Aren't we asking too much of students?**

**A.** You can't be trained to perform repetitive tasks when what's routine is

being computerized or farmed out around the world to lower-cost countries. The gap between the highest paid 20% of workers and lowest paid is now the widest ever.

**Q. Do other countries have school-to-work systems worth copying?**

**A.** Be wary of borrowing abroad. They develop institutions that aren't easily transplanted to our soil. There are, of course, some ideas we can remake in our own uniquely American tradition. The German system is a good example.

**Q. How do you measure education accurately?**

**A.** One of the best initiatives in bringing educators and employers together is the new effort to set skill standards. It's very, very important. And it's taking off like wildfire.

**Q. How broad is the school-to-work movement among employers?**

**A.** Many companies are starting — or expanding programs. I think the best ones are explicitly linked to excellence in the classroom — not just training on a job. And the best ones offer young people an opportunity for building additional skills later on in their career.

**Q. How do the funds authorized under the School-to-Work Act find their way to programs?**

**A.** With relatively few dollars of seed money, we've created a highly leveraged way of funding effective programs. Local communities are putting their own money and resources into the hopper. The idea of highly leveraged funds is working very well. It may be a new kind of federalism.

**Q. What would help the most right now to get programs going?**

**A.** Employers must be more actively involved.

Our position, word by word.

# Balance



At Philip Morris, we believe that adults have a right to choose whether or not to smoke.

But we also believe that minors should not smoke. These two issues — preserving the right of adults to make personal choices and preventing minors from having access to cigarettes — are equally important. But they should be addressed separately. It's important to maintain a balanced view so both issues get the attention they deserve.

For instance, our recently launched initiative, *Action Against Access*, is one of the most comprehensive programs ever introduced to prevent minors from having access to cigarettes. We are confident that this program will make a difference.

On the other hand, we will continue to vigorously support the right of adults to make personal choices.

Our position is that the issue of youth and cigarettes should not be used to curtail the freedom of those adults who choose to smoke.

It's important to prevent minors from having access to cigarettes. But it's just as important to respect the rights of adult smokers and nonsmokers to make individual choices.

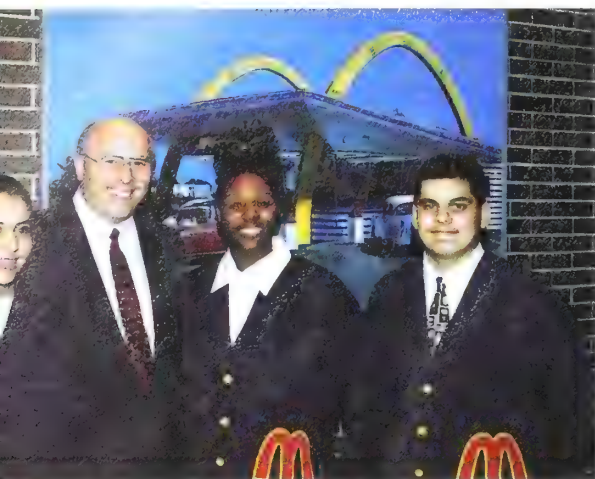


**We want you to know  
where we stand.**

#### **Facts Matter**

In June of this year, Philip Morris voluntarily stopped distributing free samples of all its cigarette brands in the United States as part of its *Action Against Access* program.





understand the applications on the factory floor and, in turn, create more realistic curriculums in school.

"We have only a few reasons for doing all this training. One is we need strategically trained people to meet global

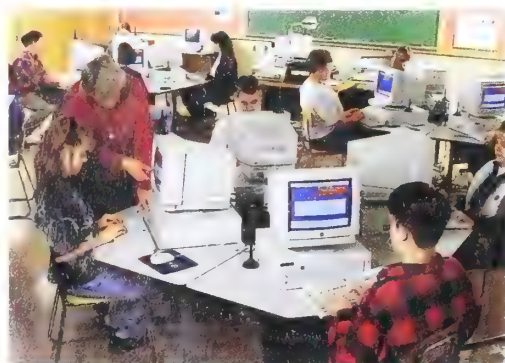
competition. Secondly, we've got to reduce our recruiting costs. We have all the horror stories of the immense expense and time involved in hiring. Lee Doyle at BellSouth put out a brochure with horror stories. I'll tell you! We have all the same stories."

Do they do it better — or just differently — overseas? Gene Bottoms, who heads the Southern Regional Education Board in Atlanta and the "High Schools That Work" program, recently visited Germany, Sweden, and Denmark with a "team of folks," including state legislators, community college administrators, and corporate executives.

"What I saw," he says, "was almost a parody of the consensus-making process. Employers and educators are so involved with each other that one can't override the other. Every time it's, 'You gotta sit down and work this through.'"

**Defining Moment.** How do those three countries define work?

"They build a framework and standards — managers, workers, educators — for the modern workplace. Not narrow standards, but ones that include quality — intellectual as well as technical.



## Case In Point

### At Apple, Information Workers are Icons

**S**ince I was in school, there have been fundamental changes in the workplace," says Terry Crane, general manager and vice-president of Apple's Education Division, which "bundles" together programs to teach business, computers, and other real-life subjects to high school students. "The skills my daughter Kristana needs are completely different from what mine were. And I now carry a cellular phone and computer to keep in touch with the work world."

#### Mobile Technology

"What's startling is the mobility of technology," Crane goes on to say. "We're all in a mobile work force-networking, using great graphics and multimedia systems, accessing databases. I wouldn't disagree with Labor Secretary Reich's formulation. Everyone — factory worker, blue-collar worker, white-collar worker — will have to be a knowledge worker. Even in an automated factory, the data and details for making repairs are on-line, available to everyone."

#### School-to-Home Links

"What's going to drive the new kind of education is the convergence of industries. Computers used to be out there doing stand-alone things. Now with mergers and buyouts — combining telecom, computers, broadcasting, and publishing companies — there are going to be new players and new jobs. Some will be in homes where more and more people will be working."

#### A Jolt from the Blue

Crane's main complaint: the lack of money to educate kids for the new cyberspace they'll occupy in the 21st century. "Schools are ready to make changes," she says optimistically. "But the funding is coming too slowly and assigned too carefully."

What's required? "When the Russians lofted Sputnik in the Eisenhower era, we recognized we were behind in science and math. It takes that kind of jolt today to get major educational programs going."

#### McMANAGEMENT:

Ed Reisi, president and CEO of McDonald's U.S.A., visits with students who are participating in McDonald's Youth Apprenticeship program. The four-year course will put some 4,000 young people on a fast track to a management career in one of the nation's burgeoning service industries.

**'Expect more from young people,' says Bottoms.**

**'We found that 40% finished high school without doing much work.'**

#### ZENITH ZEROES IN:

Students at Grayslake Community High School in Grayslake, halfway between Chicago and Milwaukee, learn computer and other high-tech skills on machines provided by Zenith Data Systems.

# Saluting A Partnership That Will Affect Generations To Come.



BellSouth is proud to salute Telephone Pioneers of America and Junior Achievement, Inc. as they join together in a mission of great importance. Beginning this year, these two organizations will work together to help broaden the education of elementary school children across the continent.

With 850,000 members, Telephone Pioneers of America is the largest industry-related volunteer organization in North America and has been actively involved in community service since 1911. In working with Junior Achievement, Inc., these volunteers will bring their work experience directly into classrooms all across North America. The Pioneers in BellSouth's nine-state area alone will dedicate over 1 million hours of community service each year to this all-important partnership. With that kind of volunteer muscle, we look forward to having a very positive impact on generations to come.



**BELLSOUTH**





## Sampling Some Top Corporate Programs

No two corporate programs are exactly alike. Here are a dozen worth examining.

### Kid Witness News by Matsushita:

Having fun while learning? Try the 'Kid Witness News' program, now barreling along in more than 200 schools in about 75 American cities. "The kids — mostly underprivileged or from minorities — write, create and produce TV shows," says the program's founder, Justin Camerlengo. "In essence, they become a TV production unit. The whole idea is to help youngsters build self-esteem. We just give schools the basics — studio equipment, teaching materials, and some guidelines."

**General Motors' GMYES:** "There's a significant disconnect between schools and work right now," says Donald I. Gray, director of the automaker's brand-new GMYES program. "Our mission is to provide a source of entry-level technicians for GM dealerships. We're earmarking some 10 schools from Oklahoma to California for starters, and we'll roll out 20 more next year." What sparked this? "Bad stereotypes. One is the parent who sees a child as a mechanic on his back on a creeper taking out engines. The problem these days aren't engines but engine controls and diagnostics. Our mechanics are now technicians in a very real sense."

### Reinventing Education at IBM:

Taking off from the title of the seminal book by chairman and chief executive Lou Gerstner, Jr., the year-old program provides grants for cities and states such as Vermont and West Virginia that use technology in new and creative ways. "We're not just putting the latest and greatest PC on someone's desk," says an IBM spokesperson. "Lou Gerstner has called for a massive overhaul of our nation's schools. This new program involves grants to rethink how."

### Toshiba/NSTA ExploraVision Awards:

It's the world's largest K-12 science

competition, backed by the Japanese portable-computer maker and the National Science Teachers Association. Students select a current technology and imagine what it might be like in 20 years, conveying their vision through a descriptive essay and storyboard. Example? A computerized toothbrush with a tiny screen in the handle to tell you if you have any cavities.

**Academy of Travel & Tourism:** It's one of the most successful offshoots of the National Academy Foundation with branches at 64 public schools in 16 cities. Its goal is right on — training young people to work in the global travel marketplace, a significant economic part of the growing service sector. Says Linda Paresky, senior vice-president of American Express, who works closely with East Boston School: "I had a senior this year who didn't think she was even going to graduate — and now she's off to college."



**ACADEMY OF TRAVEL & TOURISM:** *James Pinkston, a senior, interned at American Express with mentor George Dollar of Gold Card Account Services here looking on. Equally successful is the 13-year-old Academy of Finance, led by Sanford I. Weill, chairman and CEO of The Travelers Group*

**Cruise Controls at Zenith:** "We're offering solutions to schools — not just equipment or a product," says Lisa Collins of Zenith Data Systems. Since last May the company has been providing schools

with its CruisePad, a wireless device that acts like a keyboard and monitor to access a host PC filled with educational data. Very clever — and handy for teachers who are walking around a classroom, helping students get their work done.

**Lockheed Martin's Academy:** Of new workers entering the labor force by the year 2000, only 15% will be white males. Couple that with the demand for young people with math and science skills — only 1% of American high school students, for example, study calculus — and you can see why one of Lockheed Martin's main support programs is the Academy for Teachers of Science and Mathematics, held every summer on the campus of the University of Tennessee.

### Other noteworthy programs:

**Chrysler's World of Work,** a "job ready" program that helps K-12 students solve problems, work on teams, communicate better, and get ahead.

**Boeing Tech Prep Program,** which emphasizes quality improvement, team building, managerial skills, and adaptability to changing technology.

**Lincoln-Douglas Debates,** sponsored jointly by Lincoln Life and the National Forensic League, which sharpen the ability of high-school students to communicate by staging speech contests — inspired, of course, by the famous debates between attorney Abraham Lincoln and Senator Stephen Douglas in 1858.

**Diploma-based Performance,** an interactive program of core courseware — developed by Josten Learning — for at-risk and more fortunate students who need to learn reading, writing, math, and science in K-12 classes.

**The Arco Foundation,** a strong supporter of LEARN (Los Angeles Education Alliance for Restructuring Now) and other programs nationwide designed to close the gap between education and the workplace.



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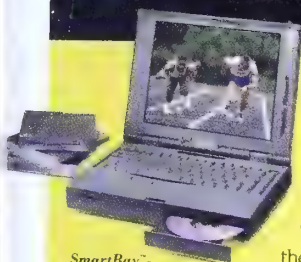
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"Those countries are a little different from each other," says Bottoms. "Germany still organizes work around some 300 occupations, from banking to automotive service. In Denmark there are around 85 standards. In Sweden they have it down to 14 standards."

All along the route the delegation found that Europeans by American standards blend work and learning without much fuss — as though it were a perfectly natural way of educating the young. This, mind you, on a continent that puts intellectual achievement on a high pedestal. It is simply not demeaning to mix practical matters with the pursuits of the mind.

"In Germany," Bottoms recalls, "we spent some time at a major bank. The managing



**WINNING AT SIFE:** *In the hot competition among Students In Free Enterprise (SIFE) held each year, the team from La Sierra University in Riverside, California won first place as 1995 International Champions — with corporate chieftains cheering its grasp of business fundamentals at an awards ceremony in Kansas City, Missouri.*

**'Europeans blend work and learning without much fuss — as though it were a perfectly natural way of educating the young.'**

## Case In Point Motorola Tells It Like It Is

**T**he trouble we've found is that schools were designed for the '40s and '50s," says Margot Brown, director of external communications at Motorola. "Factories now require skills that go beyond what schools provide. We're looking for the engineers of tomorrow — people who can think critically and solve problems."

### Productivity Push

Motorola's commitment to school-to-work goes back to the mid-'80s when the company was trying to decide whether to build a second cellular phone plant here or overseas. What kind of productivity would it get from the new plant design? Did Motorola have the "skill sets" among its workers? "We tested some of our employees," Brown recalls. "They didn't do too well by it. Then we began looking at the quality of culture right here in

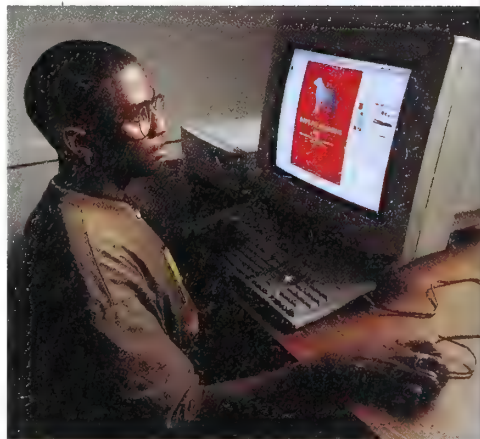
America. We went right into the school systems in Illinois, Florida, Texas, Arizona, and Massachusetts — states where we're heavily involved — and worked closely with educators. We provided them with the industry requirements of the '90s."

### Blood Transfusion

Since 1990 Motorola has had a long-term educational program that begins at the elementary level. Ed Bales, director of external education systems, maps out courses in collaboration with schools that can — and are willing to — change their curriculums. "It's enlightened self-interest," he says. "We're not doing this to cure all the social ills in the country, but to be sure we have enough engineers 20 years out. It's the lifeblood of our company."

### Think Teams

Motorola starts with District



**BELLSOUTH AS BELLWETHER:** *In DeKalb County, Georgia, the telecommunications giant is a leader in helping students learn skills to build careers.*

Leadership Learning Teams. And they build curriculums from the ground up.

"What we do is identify all the people in a school community who have something to do with the total system — it could be parents, grandparents, teachers, administrators," says Brown. "We get them to work together as a team."

"A lot of schools still have kids learn by memorization rather than understanding. But we treat them like individuals who can think for themselves."

Under Motorola's tutelage, teenagers grapple with real business problems presented to them on videotape. For example, they recently took a shot at helping Motorola set up its Iridium satellite consortium, aimed at refining global communications. Which Latin American countries should be invited into the consortium? Several student teams researched the issues, then made their presentations which proved to be surprisingly sophisticated. Says Brown, "It was positively amazing to watch!"



# Consider Those Who Walked In These Shoes



By doing just that, 785,000 students from all walks of life have learned about the dangers of racism and indifference that the Holocaust teaches us. At the United States Holocaust Memorial Museum, these shoes, now silent witnesses to the victims who wore them until moments before their deaths, teach a powerful lesson about the importance of individual responsibility in our pluralistic democracy.

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**SIEMENS PARTNERSHIP:** Barry Blystone, director of training and development at the company's North Carolina subsidiary near Raleigh, works with 'apprentice' Zeltina O'Neil to help upgrade her skills. The Siemens program includes mentoring, internships, career planning, and even going on to college.

director and three of the vice-presidents were graduates of the bank's apprenticeship program. Out of some 400 applicants, each year the bank takes about 80. They rotate through all the jobs — with an overview the first year and then specialization the second."

### Career-bound Youth.

In the "High School That Works" program that Bottoms has promoted in 20 states, students focus on math, science, and problem-solving.

In the program's prescription for a smooth

school-to-work transition are 10 basic points. Among the most important:

- Expect more from young people. "We found that 40% finished high school without doing much work," says Bottoms. "Typically, they'd say, 'I went to high school because my friends were there.'"
- Upgrade vocational classes. Do real, authentic things. "Give them tough problem to think through," says Bottoms.
- Drop every "basic" course. Go for more applied learning, more project learning.

"High performance," says Bottoms, invoking the benchmark words so often used in school-to-work discussions. "It's gotta be for everybody." ■

## Case In Point Virginia Beach: Wired Playground

For a textbook case of bringing schools up to speed in tandem with the work demands of the 1990's, listen to Dr. Pat Konopnicki, a school-to-work evangelist whose flock includes 80 public schools and 76,000 students in the Virginia Beach area, including the U.S. Navy's base in Norfolk.

### Quality Kick

"When students come through our programs, they're employable anywhere," he says. "They have an edge up, thanks to the partnership we've developed with Compaq, Novell, and a local company, Electronics Systems. What we call the Five Cornerstones of Quality in our school system are teamwork, empowerment, continuous improvement, customer service, and data-driven decisions. It's very Reich-like."

### Strong Partnership

"We first need to develop a strategic plan—a partnership of business, labor, industry and school personnel," says Konopnicki whose formal title is Director Of Technical and Career Education, Virginia Beach City Public Schools. We're fortunate in having a strong one here in Virginia Beach, including a military community."

"Whenever applicable, we've sought and applied for certification—whether it's an auto mechanic or an RN (registered nurse) or a motel/hotel operator—so long as there's a national affiliation. In Virginia Beach we believe total quality management should be taught to students. We've created a high school course called TQM. Now we're talking about a Computer Network Engineer Apprenticeship."

### Personal Networking

Dr. Konopnicki does a lot of proselytizing about how the "intellectual capacity of our work force has to increase." But he also takes to heart one of school-to-work's favorite buzzwords: teamwork. He works with the National Alliance of Business. He's in touch with Compaq and Novell. He's on the pipe to Ford and Motorola on quality issues. And after 11 kids ("not a great number, but a step") had gone through his Computer Network Administrators program, Pat took calls from admirers in 16 states and three countries who wanted to know how to create clones.

What's his opinion of the School-to-Work Opportunities Act? "It's put school-to-work on the front burner."

'After 11 kids had gone through his computer program, Pat took calls from admirers in 16 states and three countries who wanted to know how to create clones.'

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Carnegie Foundation for the Advancement of Teaching; **Mary Diez**, Ph.D, of Milwaukee, Wisconsin, Dean of Education, Alverno College; and

**Gene Bottoms**, Ed.D, of Atlanta, Georgia, Director of the Southern Regional Education Board's "High Schools That Work" program. Congratulations to three individuals whose dedication to scholarship

should be an inspiration to us all.

For more information, write: The Harold W. McGraw, Jr. Prize in Education, The McGraw-Hill Companies, 1221 Avenue of the Americas, Room 2917, New York, NY 10020.

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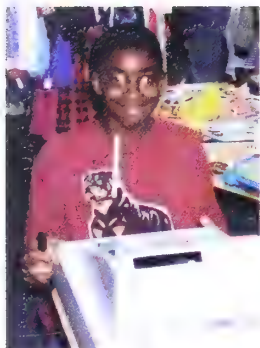
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## 1995 Awards for Instructional Innovation

### 'Break the Mold' Schools: Urban, Rural, Suburban



**F**or the sixth year in a row *Business Week* is proud to present its annual award to public schools that have worked closely with the business community to develop innovative and challenging curricula. In one form or another, the two-way cooperation has helped students make the transition from school to work much easier and more productive.

In many cases, the underpinning that leads



to success comes down to motivation. Students won't make it in the real world without wanting to.

"One student who had missed approximately eighty days during the school year improved to such an extent

that he only missed twelve days this year," says a report from Providence's Chamber of Commerce Academy, where students who achieve a C average work with full-time mentors and fill paid positions at work places in Rhode Island's capital.

"Within our school we have established a project dubbed 'Excel City' by the students," reads a critique from Berkman Elementary of Round Rock, Texas. "It's a city in miniature consisting of businesses, a governance, and a token economy run by and for the students. The role of the private sector in making this school so innovative has been extensive and far reaching."

Equally rewarding are the success stories told by the four other 1995 winners: An Achievable Dream

School of Newport News, Virginia; the Clark County Skills Center of Vancouver, Washington; Grenada Elementary of Grenada, Mississippi, and The Mat-Su Alternative School of Wasilla, Alaska.

The six winning elementary and secondary schools — two urban, two suburban, and two rural — will each receive a \$2,500 grant. Half is an honorarium for the school's innovative talent and dedication. The other half helps to cover the expenses of the award's "Network for Success" in which winners share their programs with other schools.

Last month the presentation of the 1995 awards took place in the Dirksen Senate Office Building in Washington during a "We Care" conference sponsored by the American Association of School Administrators (AASA). And now begins our search for six more winners for the 1996 awards.

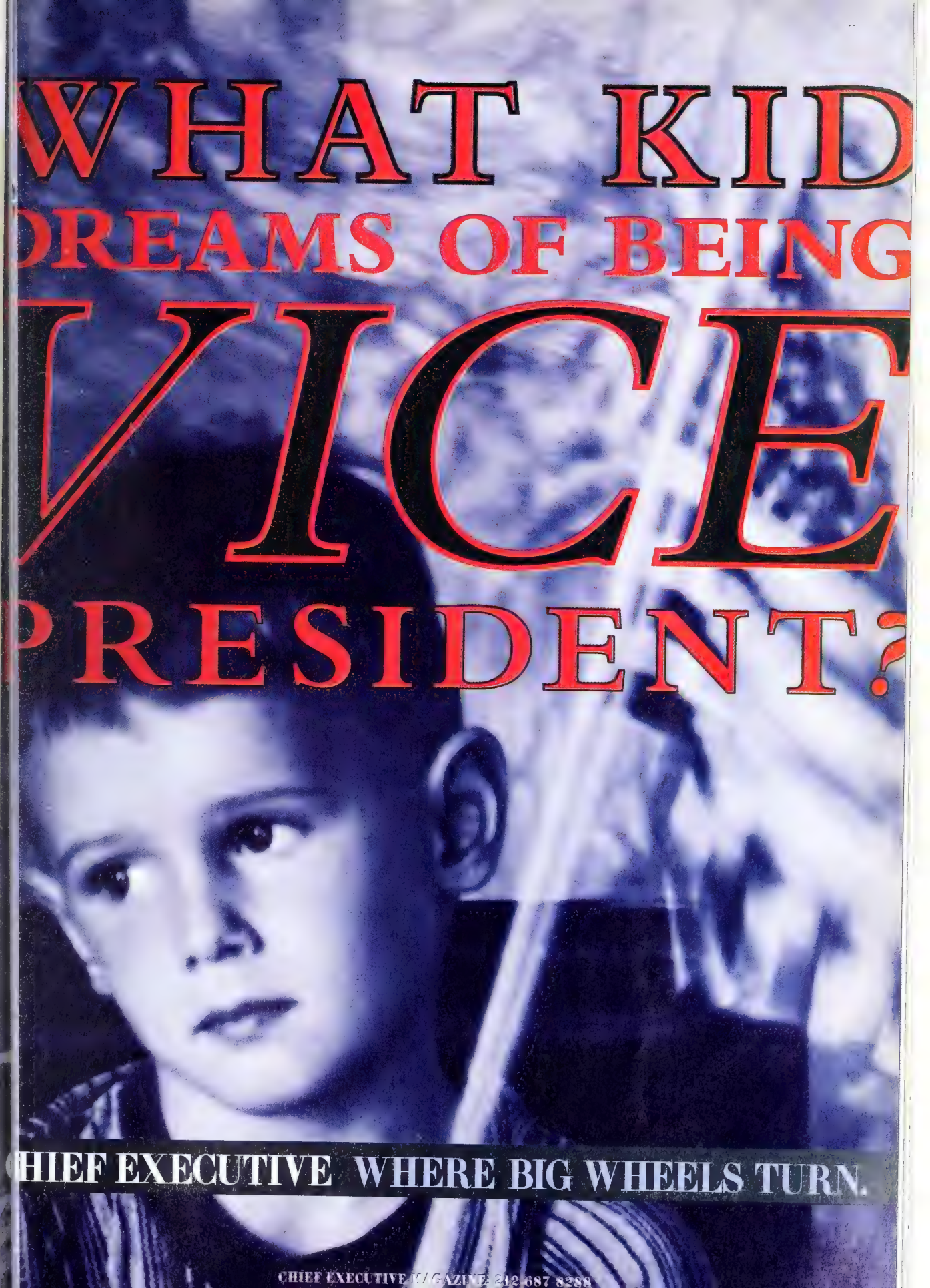
'Break the Mold' is what our schools need to do if they're going to create educational programs that reflect the realities of today's society," says David G. Ferm, publisher of *Business Week* in announcing the awards. "Our hat is off to this year's innovative winners."



**CHALLENGE:** *Classrooms come alive — and kids smile — when a school creates an educational program that connects with the real world of work and fires the imagination of young people.*





A black and white photograph of a young boy with a dreamy, upward-looking expression. He is holding a large steering wheel, suggesting he is in a car. The background is slightly blurred, showing what might be trees or a park setting.

# WHAT KID DREAMS OF BEING VICE PRESIDENT?

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**BIG PUSH:** Sweeney says he'll devote much more money to organizing

IONS

## A NEW DEAL AT THE AFL-CIO?

reformers, likely to take power, promise tougher methods

For more than a decade, beleaguered labor leaders have bemoaned the decline of unions, citing everything from antiunion management tactics to the shift from manufacturing to services. Then early last year, a group of union chiefs decided they would have to act, no matter the difficulty. In August, they forced longtime AFL-CIO President Lane Kirkland and began drawing up ambitious plans for reviving their movement. Now the reformers, headed by Secretary-Treasurer John J. Sweeney, are about to take charge of the 13 million-member federation. Sweeney and two running mates, United Mineworkers President Arthur J. Altmeyer and Linda Chavez-

Thompson, a vice-president of the government workers union, hold 58% of the votes and seem likely to defeat Thomas R. Donahue, Kirkland's longtime No. 2, in elections slated for Oct. 25. There's only a slight chance that Donahue, who had long been the heir apparent, could still win the top job.

**BETTING BIG.** Whoever wins, labor will undergo a restructuring as thorough as any in Corporate America. Both candidates vow to devote a third of the AFL-CIO's \$60 million budget to membership drives and to be more aggressive in bargaining and national politics, while slashing costs (table). Both would step up polling, advertising, and other media efforts to reposition unions in the public eye. "The point is to make

the AFL-CIO relevant again by converting it from a creaking old cold-war clock into a sleek fighting machine," says Trumka, a 46-year-old firebrand running as Sweeney's No. 2.

The question is how much difference even the most vigorous efforts will make. Sweeney is betting big on the low-wage service sector, where his union has had much success organizing such workers as janitors and health-care employees. His militant approach there won't do much for industrial workers struggling with technology and how to help companies compete globally, say some experts. "I'm not sure they have a strategy for higher-wage workers," says Cornell University labor economist Harry Katz. Still, even staunch opponents think that the jolt of new energy will at least begin to reverse labor's slide, which has cut its share of the workforce by 10 percentage points since 1975, to only 15.5% today. "I think unions have hit bottom and will go up," says John N. Raudabaugh, a former Republican appointee to the National Labor Relations Board who is now a management labor attorney in Chicago.

The new leaders' first task will be to remake the AFL-CIO. The federation today is a sprawling bureaucracy without focus. Sweeney plans to close or combine many of its 21 staff departments, which employ 375 people and handle everything from education to employee benefits. Already, Donahue has moved to consolidate four affiliated international affairs institutes, Kirkland's pet concern. Sweeney is likely to make a wholesale sweep of top staffers, many of whom aren't seen as hard-charging activists.

The federation's new mission will be to boost labor's ranks. Its own culture is no help there. The AFL-CIO is an umbrella group with no rank-and-file membership

**TRUMKA:** Turn the federation into "a sleek fighting machine"

### CHARGING HOR

Leaders poised to take over the AFL-CIO have ambitious plans for reviving unions. Some key ideas:

pend at least a third of the federation's \$60 million annual budget on membership drives

establish a separate Sunbelt organizing fund to help unions target low-wage workers in the South, where several unions have won recent drives

- Cut other expenses by consolidating 21 internal AFL-CIO departments
- Create a national center to train political campaign workers
- Set up a central office for spearheading pressure campaigns against companies engaged in bargaining

DATA: BUSINESS WEEK





## TACTICS THAT JOE HILL NEVER DREAMED OF

Hillhaven Corp. is all too familiar with John J. Sweeney's arsenal. Under his leadership, the Service Employees International Union (SEIU) has used some of the most aggressive and inflammatory tactics the nursing-home chain has seen, gripes Hillhaven labor relations director Keith M. Sherman.

Picketing and strikes are just the tip of the iceberg as the SEIU negotiates contracts at 25 of Hillhaven's

get. Last year, the SEIU intensified a nationwide campaign against the entire nursing-home industry by going after giants such as Beverly Enterprises, Sun Healthcare, and GrandCare, among others. Although the SEIU represents 75,000 nursing-home workers, that's only 7% of the nursing assistants, housekeepers, and other employees in the rapidly growing business. The union began by holding focus groups with workers

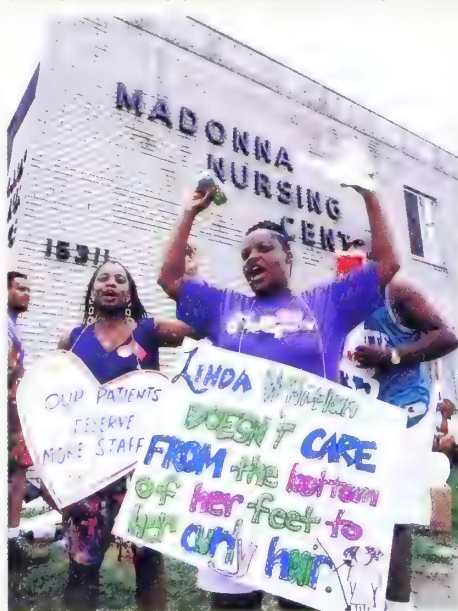
and found many concerned about inadequate patient care in an industry notorious for cutting corners. The union campaign, dubbed "Dignity, Rights, and Respect," focuses on ways that issues of quality of care and working conditions overlap.

**A PROBE.** The strategy has hit a nerve at Beverly, the nation's largest nursing-home operator: It employs 80,000 workers at 706 homes, fewer than 10% of whom are organized. The SEIU recently distributed a scathing report on the company's quality-assurance program in Missouri. And in Texas, AFL-CIO officials are trying to get the attorney general to investigate Beverly for possible deceptive-trade practices. The union points to a Beverly home in Weatherford, Tex., briefly taken over by the state in July after it had won Beverly's highest quality ratings months

before. The state noted such deficiencies as "severe weight loss to the point that residents look like people coming out of concentration camps." The company calls the situation an "isolated incident" and says the problems have been corrected.

SEIU's strategy has brought in some 5,000 new members at 100 homes since 1993, double the rate of the prior two years. There's a long way to go—at least 15,000 facilities are still nonunion. With Sweeney at the AFL-CIO's helm, nursing-home operators can expect more of the tactics they've come to dread. And employers in other industries are likely to face them, too.

By Wendy Zellner, with Stephanie Anderson Forest, in Dallas



**TIP OF THE ICEBERG:** The SEIU uses many weapons other than strikes

California nursing homes. In September, the union posted a bulletin on the Internet asking shareholders to oppose Hillhaven's merger with Vencor Inc. It also filed a federal lawsuit against the marriage, charging that Hillhaven and Vencor had included false claims in its proxy statement. Although the effort failed, the union succeeded in scaring off Health Net, California's second-largest health maintenance organization, which recently stopped referring its members to Hillhaven after the HMO found itself the target of pickets from the SEIU. "We're going to refer our members elsewhere until this labor dispute is over," says David W. Olson, a Health Net vice-president.

Hillhaven isn't Sweeney's only tar-

of its own, so Kirkland and his predecessors largely left organizing to individual unions. Even if he wins, Sweeney won't be able to tell member unions what to do, but he hopes to lead by example. Most unions devote less than 5% of their budgets to organizing. Sweeney lifted the share at his union to a third not long after he took over in 1980, and he thinks doing the same at the AFL-CIO will spur others to follow suit.

Sweeney also has specific lessons to impart. His union nearly doubled in the 1980s, to 1.1 million, largely by returning to methods used during labor's explosive growth in the 1930s. The campaigns revolve around rank and filers who contact prospective members. They link up with community and church groups to create the feeling of a social movement and to pressure employers whose resistance might intimidate possible recruits. The service union's most successful membership effort, called Justice for Janitors, has signed up 35,000 workers since 1985. "These organizing methods work a lot better than others," says Kate Bronfenbrenner, a labor expert at Cornell University who has studied membership drives.

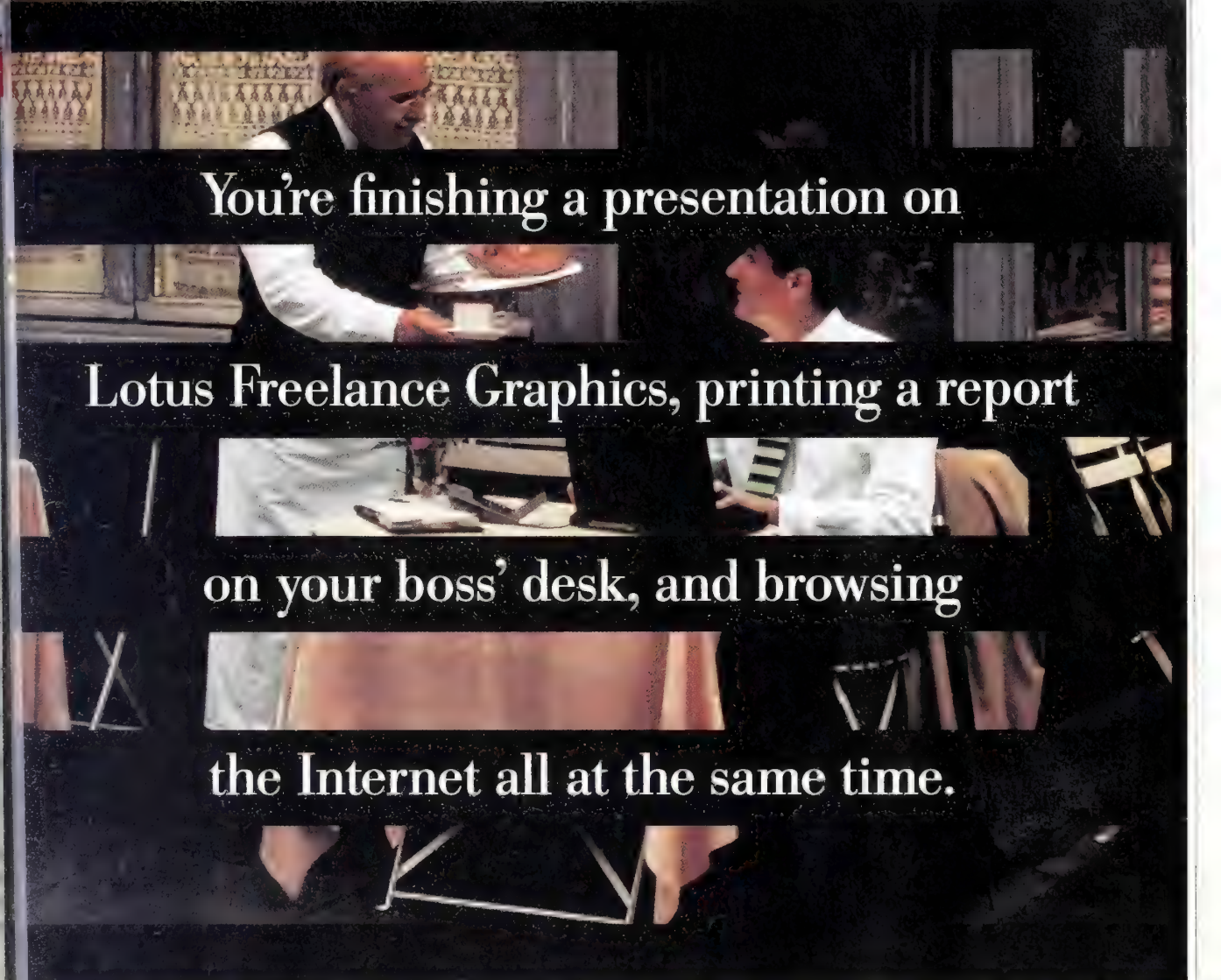
**SUNBELT DRIVE.** Employers in the anti-union South are likely to see the most new organizing activity. In recent years, textile and food unions have targeted low-wage industrial workers there. Sweeney wants a special Sunbelt organizing fund to coordinate regional membership drives.

Labor's political efforts will become more visible as well. Sweeney hopes to set up a national center to train union members to work on political campaigns. Sweeney doesn't rule out eventually supporting efforts towards a labor party, which a number of union leaders have begun to promote. But he thinks unions should first concentrate on honing their message and recruiting sympathetic candidates. "Why shouldn't union members be candidates where they have the support of a lot of the community?" he asks.

Labor still faces tough going in the next decade, particularly since many employers don't accept unions as a legitimate part of the economic landscape. Still, union membership already has stopped falling in the past three years, in part because of the renewed vigor of a handful of larger unions. The AFL-CIO can't force the rest to jump on the bandwagon. But its new leaders need to generate enough momentum to propel them along if the AFL-CIO is one day to reclaim its former title: Big Labor.

By Aaron Bernstein in New York





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# THE CASE AGAINST MERGERS

## Even in the '90s, most still fail to deliver

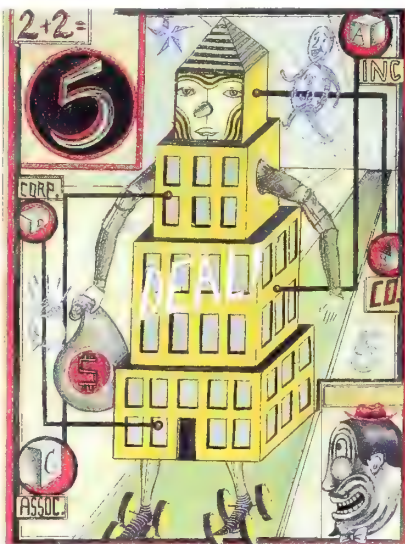
**A**merican companies are in the grip of full-blown merger mania. In the first nine months of the year, according to Mergerstat, a merger research service, the value of all announced deals reached \$248.5 billion, surpassing by a hairbreadth the record full-year volume of \$246.9 billion for 1988. The number of transactions valued at more than \$100 million will likely top the record 383 announced last year.

Leading the pack are banks, health-care providers, computer-software concerns and media, communications, and entertainment giants. Lately, consolidation in the utility and insurance industries has picked up steam.

**BURDENS.** This historic surge of consolidations and combinations is occurring in the face of strong evidence that mergers and acquisitions, at least over the past 35 years or so, have hurt more than helped companies and shareholders. The conglomerate deals of the 1960s and 1970s that gave rise to such unwieldy companies as ITT Corp. and Litton Industries have since been thoroughly discredited, and most of these behemoths have been broken up.

The debt-laden leveraged buyouts and bust-ups of the 1980s didn't fare any better, and many surely did a whole lot worse. That era ended not with a whimper but with a bang: In October, 1989, when bankers couldn't raise the money for the ill-conceived buyout of UAL Corp., the deal collapsed, dragging the stock market down with it.

But by the 1990s, chief executives and investment bankers figured that they had finally gotten it right. If UAL marked the end of the 1980s crazy season, then the July, 1991, announcement by Chemical Bank Corp. and Manufacturers Hanover Corp. that they would join in a \$2.3



billion stock swap to create the nation's second-largest banking company and produce \$650 million in annual expense savings by 1994, seemed to signal that the Age of Reason in mergers and acquisitions had begun. This was to be the era of strategic deals—friendly, intelligent and relatively debt-free transactions done mostly as stock swaps, which were supposed to enrich shareholders by producing synergies in which two plus two would equal five or more. These synergies would take the form of economies of scale, improved channels of distribution, greater market clout, and ultimately higher profits for surviving companies. Although Harvard University's Michael Porter in a seminal May, 1987, *Harvard Business Review* article argued persuasively that most would-be deal synergies are never realized, the new strategic

transactions, Wall Street promised, would be different.

It turns out they're not. Indeed, with investment bankers singing their new, improved siren song, many big company CEOs are demonstrating that they still are as vulnerable to the latest fad as the most naive individual investor.

### Why Mergers Don't Work

- Inadequate due diligence by acquirer or merger partner
- Lack of a compelling strategic rationale
- Unrealistic expectations of possible synergies
- Paying too much
- Conflicting corporate cultures
- Failure to move quickly to meld the two companies

**OFF THE MARK.** An exhaustive analysis by BUSINESS WEEK and Mercer Management Consulting Inc., a leading management consulting firm, of hundreds of deals completed in the first half of the decade indicates that their performance has fallen far short of their promises. Deals that were announced with much fanfare such as AT&T's 1991 acquisition of NCR and Matsushita's 1991 acquisition of MCA, have since unraveled. Others, including KeyCorp's 1994 merger with Cleveland's Society National Bank, acquisitions by big pharmaceutical manufacturers of drug wholesalers, as well as software and entertainment deals are producing the results the acquirers had







hoped for—nor are they likely to produce good results in the future.

The anecdotal findings are supported statistically. The BUSINESS WEEK/Mercer analysis indicates that companies performed better in the wake of '90s deals, most of which have been done ostensibly for business reasons, than they did after

'80s transactions, a high proportion of which were financially driven. But the analy-

sis also concluded that most of the '90s deals still haven't worked. Of 150 recent deals valued at \$500 million or more, about half destroyed shareholder wealth, judged by stock performance in relation to Standard & Poor's industry indexes. Another third contributed only marginally to it. Further, says James Quella, director of Mercer Management Consulting, "many deals destroy a lot of value." Mergers and acquisitions, he declares, "are still a slippery slope."

Using a large sample and comparing total return three months before the merger announcements with returns up to 36 months afterward, the analysis used the S&P industry indexes to filter out, as much as possible, other external events affecting acquirers' returns. Though the data obtained with the Mercer methodology, which has been used by many students of M&A performance, are not perfect, they are considered a good proxy for the impact of mergers on buyer returns.

Deal performance has been poor because melding two companies is enormously difficult and only a few companies are very good at it. One reason is that buyers often stack the odds against success by rushing headlong into mergers and

acquisitions for the wrong reasons in search of synergy that don't exist. To make matters worse, they often pay outlandish premiums that can't be recovered even if everything goes right. And finally—and this is the real deal-killer—they fail to effectively integrate the two companies after the toasts have been exchanged. Good postmerger integration rarely makes a really bad deal work, but bad execution almost always wrecks one that might have had a shot. Says Kenneth W. Smith, a Mercer vice-president based in Toronto: "The deal is won or lost after it's done."

**EXPECTATIONS.** While it's too early to pass final judgment on some recently announced but not-yet-completed megadeals, they seem iffy as well. The planned takeover of Turner Broadcasting by Time Warner, itself a value-destroying combination, and Disney's proposed acquisition of Capital Cities/ABC lead

many media-industry observers scratching their heads over where the gains are going to come from. "For all these deals to work out, you have to believe that the American public is underentertained," says William L. Ross, senior managing director at Rothschild Inc.

In other key findings, the analysis indicated that:

- Most transactions fall below expectations, but an even greater percentage of companies lose in the M&A game. That's because a few large, inefficient acquirers, such as General Electric Co. and Dover Corp. (BW—Jan. 23), tend to do a

lot of successful deals while a much larger number of less active companies execute one or two unsuccessful mergers. In the years ending July 31, 72% of companies that completed six or more deals valued over \$5 million each yielded returns above the industry average, compared with 54% of companies that closed just one to five transactions.

- Nonacquirers are more likely to outperform their respective industry indices than are active acquirers (page 136). On



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premium...  
the clock is  
ticking on the

extra money you've paid."

## PHARMACEUTICALS

# NOT THE BEST PRESCRIPTION FOR GROWTH

**W**hipsawed by health-care reform and pressure on prices, drug-makers Merck, Eli Lilly, and SmithKline Beecham together shelled out \$13 billion for independent middlemen to boost drug sales in the last couple of years. But now, with reform dead, the deals for the so-called pharmacy benefit managers (PBMs) look like costly overtreatment. Getting a return on investment "is going to be very difficult," says McKinsey & Co. principal William Huyett. The lesson for drug-makers may be that buying their way toward growth can be misguided.

It's all a far cry from 1993, when Merck & Co. paid \$6.6 billion for Medco Containment Services Inc. Before the deal, feisty Medco played Merck against

rivals to get low prices, using its power to phone doctors and have them switch patients to competitors' medicines. By buying Medco, Merck bet it could snare a selling edge. Later, SmithKline made the same bet, buying Diversified Pharmaceutical Services, and Eli Lilly & Co. followed with its purchase of the PCS unit of McKesson Inc.

But regulators soon got nervous. Lilly's PCS unit was forced by the Federal Trade Commission to handle drugs from all makers, not just



Lilly. Worse, blocked from data with Lilly's rivals' prices, marketing strategies. Soon Merck and SmithKline all the same rest and boosting share for a price drugs was not so easy. Wash "changed the grouses a for senior PBM executive. "The sys-

that everybody anticipated total appeared."

Now some customers are pro-



# A Merger Report Card: D+

## MOST BIG DEALS DON'T DELIVER

INSTANTLY ERODED SHAREHOLDER RETURNS

30%

MODERATE SOME RETURNS

20%

EATEN ONLY MARGINAL RETURNS

33%

EATEN SUBSTANTIAL RETURNS

17%

Sample covers 150 deals worth more than \$500 million from 1990, through July, 1995. Based on total stock returns in three months before deal announcement up to three years after announcement and relative to industry indexes.

## A FEW EXPERIENCED ACQUIRERS OUTPERFORMED INEXPERIENCED ONES

Experienced

72%

Of companies that closed six or more deals, 72% had returns above industry averages. Those companies constituted 24% of a group of 248 acquirers.

Inexperienced

54%

Of companies that closed five or fewer deals, 54% had above-average returns. They constituted 76% of the acquirer group.

Data covers 1,046 deals worth more than \$5 million from Jan., 1990, through July, 1995.

## NONACQUIRERS OUTPERFORMED ACQUIRERS

Nonacquirers

69%

Acquirers

58%

Among nonacquirers, 69% produced returns superior to industry indexes, while only 58% of acquirers produced superior returns.

Sample consists of 248 companies that were acquirers and 96 companies that made no acquisitions during the period. Data covers deals worth more than \$5 million from Jan., 1990, through July, 1995.

DATA: MERCER MANAGEMENT CONSULTING, STANDARD & POOR'S COMPUSTAT, SECURITIES DATA CO., BUSINESS WEEK

At least a third of the nation's 500 largest companies have not made a single acquisition larger than \$5 million so far this decade. But from Jan. 1, 1990, through July 31, 1995, 69% of companies that made no acquisitions larger than \$5 million outperformed their respective Standard & Poor's industry indexes. Only 58% of all acquirers did better than their industry indexes. Many companies—notably Andrew Corp. and Coca-Cola Co.—whose industry rivals are bent on growing through acquisitions, have delivered superior returns by keeping investors' bankers at bay and sticking to their knitting.

**LESSONS.** To be sure, some strategic transactions, such as the Chemical-Manny Hanny merger and Primerica's October 1993 acquisition of Travelers Corp., have lived up to expectations. Toymaker Mattel Corp.'s \$1.15 billion acquisition in February of Fisher-Price has worked out well. And analysts say while the \$1.12 billion that Campbell Soup paid in February 1995, for Pace Foods was steep, the deal will likely pan out. But the kinds of mergers and acquisitions with a better-even shot at success are limited indeed. Small and mid-size deals—notably leveraged "buildups" in such fragmented industries as funeral homes and health clubs—frequently fail. The best acquisitions, says Harvard's Porter, involve "filling," including those in which one company buys another to strengthen its product line or expand its territory.

"Globalizing" acquisitions, such as those that enable companies to expand their core business into other countries, may make sense, though culture and language problems undermine many of these deals (page 132). Mergers of direct competitors aimed at dominating a market, such as marriages of big banks with overlapping branches, often have worked out.

Failures, though, outweigh the successes. Many deals are poorly thought out, founded on dubious assumptions about the potential benefits by CEOs with questionable motivations.

Some academics lately have even tried to quantify what many have long sensed intuitively: that some of the priciest deals are motivated at least in part by CEO hubris. A recent Columbia University business school study suggested that the bigger the ego of the acquiring company's CEO—as reflected in such things as relative compensation and media praise—the higher the premium the company is likely to pay. Although some have questioned the methodology, many agree with the conclusions.

"There's tremendous allure to mergers and acquisitions," says Porter. "It's the big play, the dramatic gesture. With the stroke of a pen you can add billions to size, get a front-page story, and create excitement in the markets."

Other emotions also play a role. First Chicago Corp.'s Richard L. Thomas may not have been driven by personal hubris as much as by civic pride. Some contend he rushed into merging with NBD Bancorp, parent of National Bank of Detroit, in July out of fear of being bought out by voracious NationsBank. "His goal was to keep a Chicago bank in Chicago," says one bank insider.

**GOOD MONEY.** Optimism is bolstered by a variety of rationales. One is that vertical integration—linking manufacturing with distribution—will yield vast synergies. On that theory, Merck, Eli Lilly, and SmithKline paid handsomely for drug wholesalers, but the prospects for those deals are looking bleaker and bleaker (page 124). Such linkages are behind the Hollywood deals, such as Disney's acquisition of Capital Cities/ABC. "I hate to use the 's' word," says Disney Chairman Michael Eisner, "but that's synergy at work." Others are skeptical. Says Tele-Communications Inc. CEO John C. Malone: "It's an industry that's as certain as betting on a race horse."

Numerous companies have blundered lately when they tried to engineer a major redefinition of their businesses

1. In July, the Teamsters' Consolidated Tri-State Joint Fund bought Medco and signed up its members with Express Scripts in Missouri PBM. "We wanted everything completely independent," says state executive director Rose-Coudry.

**RETURNS.** A payoff looks doubtful. Food & Drug Administration regulations relating the captive PBMs, including Lilly and IMS America, the prescription-tracking service, say produced little or no rise in returns for parent-company drugs. SmithKline's antidepressant Paxil on market-leading Prozac, but diluted the company's sales force because of its newness. And Merck's heavy marketing of the cholesterol-lowering Zocor hasn't stopped sharp sales. Andando Ltd.'s half-price comedy, Lescot.

Companies insist the payoff will

come. Argeris N. Karabelas, North American president for SmithKline, doesn't know when SmithKline will get back the \$2.3 billion it paid, but he argues that DPS will drive growth. Lilly's North American pharmaceuticals president Mitchell E. Daniels says just when PCS pays off will turn on whether Lilly finds an equity partner to share the \$4.1 billion cost. Merck executives declined comment, but a spokesman says Medco is profitable.

Still, the odds of a full return have lengthened. Says James A. Quella of Mercer Management Consulting Inc.: "It's an uphill battle to justify the kind of (PBM purchase) numbers we're talking about." A former senior PBM executive says the parents will turn the units into low-profile managed-care marketing arms or even seek buyers in a few years. The problem: Who will pay a few billion then for a used PBM?

By Joseph Weber in Philadelphia



# One study suggests the bigger the ego of the acquiring company's CEO, the higher the takeover premium

through merger and acquisition—often in response to sea changes in regulation, technology, and even geopolitics. If the spate of copycat deals in computers, telecommunications, media, and technology are any indication, these companies seem to fear they will be left behind forever if they don't do something and do it fast. "Nobody wants to be marooned,"

says David A. Nadler, chairman of Delta Consulting Group.

## Special Report

In 1991, when AT&T succeeded in taking over computer maker NCR, it figured it had won a major victory in its dream of linking computers and telecommunications. As things turned out, the dream proved to be wishful thinking. Moreover, sources familiar with the marriage say that AT&T may have erred by taking a hands-off approach. Ironically, when NCR later acquired Teradata Corp., it blew away some of the company's most creative people.

Harsco Corp., a diversified manufacturer based in Harrisburg, Pa. succeeded in expanding its steel mill service business globally with its \$400 million acquisition of Mulco International. But it still stumbled in trying to turn swords into plowshares with a tiny deal. When Harsco lost its U. S. Army contract to supply five-ton trucks, it paid \$1 million to a defunct school-bus company in a bid to salvage the truck plant, which was now making trucks for export. "The startup period was too slow, production costs were too high, and Harsco failed to gain market penetration," says Harsco Chairman Derek C. Hathaway. Meanwhile, foreign truck deals fell through. In 1994, Harsco moved to close the plant and charged off \$8 million.

Although consolidation of health-care providers has made sense for some, it certainly didn't for Dallas-based Medicare International Inc. and Critical Care America, based in Westborough, Mass. If ever there was a marriage made in he-

## SOFTWARE

### CLICKING ON *MERGE* ISN'T ENOUGH

In the information-technology industry, blink and you might miss the next big trend. No surprise, then, that tech companies have been among the most active dealdoers. In the first half of 1995, deal volume jumped 76%, to 649, for a record \$39.3 billion, according to Broadview Associates, a merger adviser.

In the fast-paced software market, it's often quicker for companies to buy products than to spend years developing their own. And size is an important advantage, so companies are joining forces to broaden product lines and cut costs. The synergies are so great, these companies figure, that they're willing to pay huge premiums for their prizes. The biggest: In July, IBM paid \$3.5 billion, or \$64 a share, for Lotus Development Corp., about twice the preannouncement price. IBM was after Lotus' popular Notes "groupware" program, which it thought could give it a strategic edge in the high-growth market for networked software; analysts called the deal brilliant.

Will big premiums pay off? It's too soon to know for sure. But history

has shown that strategic technology deals, while they may make sense on paper, are tough to carry out. "People do these deals as big strategic visions, and they forget that what makes them work are all the details," says Gordon E. Eubanks Jr., chief executive officer of Symantec Corp., which he built into a \$335 million software company by a series of acquisitions. That's especially true in software, where brainpower counts for more than horsepower.

One of software's most ill-starred acquirers is Borland International Inc., a maker of languages. In 1991, Borland paid \$440 million for Ashton-Tate Co., then the dominant supplier of personal-computer database software. But Ashton-Tate had started to fall behind by then, and product delays continued under Borland. Borland's inability to digest the acquisition sank it, some say. Borland went on to report huge losses for four straight years.

Attention to detail won't help if the strategic vision behind an acquisition is flawed. Take Novell Inc. In the early '90s, under then-Chairman

Ray Noorda, Novell set out to beat Microsoft. No matter that Novell was the dominant supplier of networking software. Noorda was determined—some say obsessed—to match Microsoft's every move, a flawed strategy, it turns out.

**STEAMROLLED.** In 1991, Novell bought Digital Research Inc., which made DR-DOS, a PC operating system that competed with Microsoft's popular MS-DOS. In 1993, it snatched up Unix System Laboratories, which developed the Unix operating system, for \$320 million. In June, 1994, came the \$855 million acquisition of WordPerfect Corp., developer of the leading word processing program.

When Novell bought WordPerfect, its market was already under siege from Microsoft. It now has 90% of the market for "suites" that include word processing programs; Novell's share is 5% and falling. "Microsoft has been rolling over WordPerfect for three years now," says Charles Federman, a Broadview managing director.

Novell's other deals fared poorly, too. It has discontinued development of DR-DOS, and on Sept. 20 sold its languishing Unix business for just \$72 million. Now it's refocusing on its core networking business—lest Microsoft grab that, as well. Concentrating on the core business is a strategy a lot of other software players might consider.

By Amy Cortese in New York





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this September, 1992, combination of the nation's largest surgery-center chain and largest independent operator of home intravenous services was it. The concept—to create a hospital without walls and enable Medical Care America to profit from the rising demand for low-cost outpatient services—certainly sounded good. But virtually everything that could go wrong in a merger went wrong in this one. Poor timing, faulty due diligence, culture clashes, and big egos doomed the deal from the start. The merger took place just as intensified competition began driving down prices for home infusion services. Critical Care's problems were masked by slow insurer payments and infrequent internal reporting, which made it difficult to spot trends.

Less than three weeks after the merger, Chairman and CEO Donald E. Steen announced that third-quarter 1992 results would fall below expectations, triggering a free fall in Medical Care America's shares.

Management responded by slashing Critical Care's staff, which, in turn, caused it to lose customers. Shareholder lawsuits followed. "The Critical Care merger was bad, really bad," says Steen. "It's something I'm trying to forget." In March, 1994, Medical Care America sold off Critical Care to Caremark International Inc. and six months later sold out to Columbia/HCA Healthcare Corp. for \$850 million. "This has been a very good merger," Steen says, largely because its broad geographic coverage and supply contracts have enabled it to lower prices.

**CHAPTER 11.** Other attempts at expanding by acquiring closely related companies have also bombed. Take, for example, Kmart Corp.'s early 1990s acquisitions strategy. Instead of focusing on its core discount business, it lost more ground to Wal-Mart Stores Inc. when it diverted its attention and capital to buying up fast-growing specialized retailers, sometimes paying top dollar. By yearend 1992, Kmart had become a \$30 billion-sales retail conglomerate with seven specialty store chains and 2,300 Kmart stores. But overhead was higher than rival Wal-Mart and sales per square foot lower. "The Kmart stores were totally neglected," says Trish Reopelle, an analyst with the State of Wisconsin Investment Board. A year later, Kmart was forced to begin selling its specialty stores and



## JAMES QUELLA Mercer Management Consulting

"Many deals destroy a lot of value." Mergers and acquisitions, Quella declares, "are still a slippery slope."

premium for an opportunistic acquisition, you ought to know [that] on average, it's not going to work. It's not going to even back its cost of capital."

What's an excessive acquisition premium? Says Sirower, "Because synergies are so difficult to achieve even with sound strategy, once you cross the 25% threshold, you're really piling on the risk." If Sirower is right, then a lot of companies are gambling heavily. So far in 1995, according to Mergerstat, average premiums on deals over \$500 million was about 37%, down from about 41% last year but up dramatically from 26% in 1993.

Companies, Sirower says, already are forced to compete hard that it's difficult to produce large gains in returns and profitability. "But if you pay a premium, you've got to compete even better." Meanwhile, he says, "the clock is ticking on the extra money you've paid." In his dissertation, Sirower concluded that to recover, say, a 5% acquisition premium, a buyer who began realizing synergies in the second year would have to, in effect, increase the return on equity of the target by 12 percentage points in the second year and maintain that over the next nine years—just to break even.

That makes Time Warner Inc.'s \$7.5 billion offer for Turner Broadcasting System Inc. appear even more bizarre. Says Mercer's Quella, "Turner overpaid for much more than what he bought, and now Time Warner is paying a premium on top of that."

Although buyers think they may be doing the smart thing by buying a company in a related business, the Mercer analysis found that because they pay higher premiums than they do for companies in unrelated businesses, they leave the advantages of related acquisitions on the negotiating table.

But most experts say that the deal-breaker is usually bad postmerger planning and integration. They generally agree that if a deal is

### The Worst Megadeals of the 1990s

| ACQUIRER/ADVISER                     | TARGET                | VALUE IN \$BILLIONS | COMPLETED | CAGR* |
|--------------------------------------|-----------------------|---------------------|-----------|-------|
| MEDICAL CARE INTL<br>FIRST BOSTON    | CRITICAL CARE AMERICA | .85                 | 1992      | .055  |
| QUAKER OATS<br>LAZARD FRERES         | SNAPPLE BEVERAGE      | 1.70                | 1994      | .726  |
| NOVELL<br>MORGAN STANLEY             | WORDPERFECT           | 1.42                | 1994      | .773  |
| TIME INC.<br>WASSERSTEIN/SLH         | WARNER COMMUNICATIONS | 12.84               | 1990      | .790  |
| BANKAMERICA CORP.<br>MORGAN STANLEY  | SECURITY PACIFIC      | 4.21                | 1992      | .892  |
| COSTCO WHOLESALE<br>DONALDSON LUFKIN | PRICE CO.             | 1.57                | 1993      | .951  |
| ELI LILLY<br>LEHMAN BROS.            | PCS HEALTH            | 4.10                | 1994      | .971  |
| AT&T<br>MORGAN STANLEY               | NCR                   | 7.53                | 1991      | 1.020 |
| MILLER BANK CORP.<br>GOLDMAN SACHS   | BOSTON CO.            | 1.45                | 1993      | 1.077 |
| MATSUSHITA<br>NOMURA WASSERSTEIN     | MCA                   | 7.41                | 1991      | NA    |

DATA: BUSINESS WEEK, SECURITIES DATA CO., S&P'S COMPUSTAT

\*CAGR: Compound annual growth rate in market value divided by industry index, based on acquirer total return 3 months before announcement and 36 months thereafter, or longest time period available

## Special Report

# WHY LTCB?



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stand any chance of success, companies must move quickly and decisively to appoint the new management team, cut costs, reassure customers, and resolve cultural conflicts.

First Chicago's planned merger with NBD has some insiders wondering whether these two disparate corporate cultures—a freewheeling money center institution that serves large corporations, and NBD, a conservative middle-market lender—can possibly work together. Four months into the merger, insiders say lines of

management responsibility and authority are still unclear. Said

one senior executive: "The people in Chicago think they are being taken over by Detroit, and the people in Detroit think they are being taken over by Chicago."

Few deals made more sense on paper yet so little sense culturally than the October, 1993, merger of Price Club and Costco Wholesale to create Price/Costco Inc., which became the second-largest operator of warehouse clubs after Wal-Mart's Sam's Club. "The economies of the two companies coming together to compete with Sam's Club were compelling," says Jeffrey Atkin, principal of the Seattle money-management firm of Kunath Karren Rinne & Atkin.

The deal had many problems, but the worst were cultural. The Price and Costco people just didn't seem to hit it off. Says analyst Michael J. Shea of Charter Investment Group:

"The Price guys had much more of a real estate strip mentality. The Costco guys were the type who started working at grocery stores bagging groceries when they were years old and worked their way up the ladder." In one of the shortest corporate marriages ever, Price and Costco broke after less than a year, in August, 1994. Says analyst M. B. Byl, of Laird Norton Trust Co.: "The best thing to happen to that marriage was the divorce."

All this indicates that many large-company CEOs are making multibillion-dollar decisions about the future of their companies, employees, and shareholders in part by the seat of their pants. When things go wrong, as the evidence demonstrates that they often do, these decisions create unnecessary tumult, losses, and heartache. While there clearly is a role for thoughtful and well-conceived mergers in American business, all too many don't meet that description. Moreover, in merging and acquiring mindlessly and flamboyantly, dealmakers may be eroding the nation's growth prospects and global competitiveness. Dollars that are wasted needlessly on mergers that don't work might better be spent on research and new-product development. And in view of the growing number of corporate divorces, it's clear that the best strategy for most would-be marriage partners is never to march to the altar at all.

*By Phillip L. Zweig in New York, with Judy Perlman Kline in Pittsburgh, Stephanie Anderson Forest in Dallas, and Kevin Gudridge in Seattle*

## BANKING

# A BANK-EAT-BANK WORLD—WITH INDIGESTION

**W**hen the news broke on Aug. 28 that Chemical Banking Corp. and Chase Manhattan Corp. had a \$10 billion plan to merge, investors sent their stocks soaring. "What we've created is an unusually well-diversified mix of businesses, where we have leadership positions almost across the board," exulted Chemical Chief Executive Officer Walter V. Shipley.

Look again. The banks expect to cut costs by a hefty \$1.5 billion and eliminate 12,000 jobs. But they have yet to detail plans to increase revenues—a much harder chore. And some analysts are fretting about the deal's complexity.

**SORRY TRACK RECORD.** Shipley says those challenges are "more than offset" by Chemical's experience with mergers. However, pitfalls lurk everywhere when banks combine hard-to-value intangible assets, particularly in the current bank-merger frenzy. "On paper, all these deals look pretty encouraging," says Judah



Kraushaar, an analyst at Merrill Lynch & Co. But, he adds, particularly for deals assuming big revenue gains, "the risk of some of these deals not being 100% executed [as planned] is going to grow."

One reason for skepticism is the sorry record of past deals. Case in point: BankAmerica Corp.

and Security Pacific Corp. When BofA swallowed its largest competitor in 1992, it gained market position and cut \$1.2 billion in costs. But BofA also had to write down \$5 billion in assets as the California economy soured and take merger-related charges of \$449 million—together more than Security Pacific's net worth.

Today, BofA is back to respectable levels of profitability. CEO Richard M. Rosenberg says: "The strategy we put in place in 1992 has clearly begun to pay off." But some unhappy investors have been seriously frustrated in the process.

BofA is hardly alone. Less than three months after the \$5.4 billion deal between First Union Corp. and

First Fidelity Bancorp was announced, First Union said it would boost its one-time merger charge from \$140 million to \$270 million. First Union says its deal experience will help it quickly reach its targets. But some analysts are questioning the deal's strategic merit.

KeyCorp's 1994 merger with Society Corp. hasn't been easy either. Although cost savings have been substantial, "we did not get the revenue enhancements as quickly as we hoped," says KeyCorp Chief Operating Officer Henry L. Meyer III.

Some bank mergers have worked well, particularly in-market deals. Take Chemical's 1991 merger with Manufacturers Hanover Corp. Some \$750 million in costs were eliminated, and Chemical is now a leader in several key businesses. There is also a strong macroeconomic argument for bank mergers: They help wipe out chronic excess capacity.

For shareholders and bankers, though, bank deals are at best a mixed bag. Despite the rush to merge, bankers should take a very skeptical look at whether the conventional wisdom might not really be closer to folly.

*By Kelley Holland in New York, with Sam Zuckerman in San Francisco and bureau reports*



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# THE WORLD IS NOT ALWAYS YOUR OYSTER

Why cross-border mergers so often come to grief

It was a tragic ending to a story that began hopefully. Bangkok-based Unicord PLC, one of the world's biggest fish processors, spent \$280 million in 1989 to buy Bumble Bee Seafood Inc., a San Diego tuna canner whose name is known around the globe. Combining Unicord's clout in supplying fish from Asian waters with the world's No. 3 tuna brand seemed like a brilliant stroke of vertical integration. But by this year, a potent combination of marketing mistakes, some \$200 million in acquisition debt, and bad luck had driven Unicord founder Dumri Kornanthakiat to despair. Bank creditors were beating down the door, competitors were matching his every price move, and Bumble Bee was still in the red. On June 13, 43-year-old Dumri committed suicide, shooting himself

tions in general," says Susan Schneider, professor of human resources management at the University of Geneva's business school. "For cross-border deals, the value is even harder to measure." According to a study of cross-border mergers among large companies by consultants McKinsey & Co., nearly 40% end in total failure, with the acquiring company never earning back its cost of capital.

The logic of international mergers has always seemed compelling. Acquiring existing production or distribution abroad tends to be cheaper and easier than starting from scratch. For instance, although Coca-Cola Co. was already deriving 62% of sales abroad in 1981, a campaign of investing in foreign bottlers has helped it cement its leadership position

**BERND  
PISCHETSRIEDER**  
BMW

"We will need five years to get [Rover productivity] to the levels we need them to be"

in his Bangkok office. His company is now on the block.

Most cross-border deals don't end in bloodshed. But as falling trade and regulatory barriers around the world prompt more and more companies to "go global," many find they pay a heavy price for buying their way into a foreign market. On top of the usual challenges of acquiring a company—paying a fair price, melding two management teams, and capturing the elusive "synergy" that's supposed to light up the bottom line—special risks and costs attach to cross-border mergers (table, page 134). They often involve wide differences in distance, language, and culture that can lead to serious misunderstandings and conflicts.

"There's a real question about the value added of acqui-



si- abroad vis-à-vis PepsiCo. In markets where Coke lags, such as Eastern Europe, heavy spending on distribution helped it to overtake its archrival.

Logic doesn't always translate into profits, however. The Bridgestone Corp.'s 1988 acquisition of money-losing Firestone Tire & Rubber Co. The Japanese tire maker paid \$2.6 billion for Akron-based Firestone, a rich price that left observers agape. But Bridgestone, then the world's third-largest tire maker, was eager to solidify its global status and its position in the U.S. as more Japanese carmakers set up shop there.

Strategically smart as the deal might have been, it



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# The Japanese are a glaring case of the "hubris effect": They have lost \$320 billion buying U.S. trophy properties

unlikely to pay off financially for a long time. Firestone's new owners, inexperienced with operating abroad, initially kept existing management in place rather than putting in fresh leadership at the troubled company. Poor marketing that downplayed the Firestone name left U.S. consumers confused. Firestone lost \$1 billion in the first five years after the deal. And on top of the purchase price, the Japanese had to invest more than \$1.5

## Special Report

billion to upgrade Firestone plants. Better marketing has finally turned the company in the right direction, but a lengthy strike last year cost Bridgestone/Firestone \$80 million in lost profits. For the year, the company made just \$29 million on sales of \$5.67 billion. Predicted earnings of \$100 million in 1995 will only begin to put a dent in accumulated losses.

Even more compatible deals tend to require a lot more patience than expected. When German carmaker BMW in early 1994 paid \$848 million for Rover Group Holdings PLC, Britain's last major independent auto producer, many analysts hailed the combination. With the acquisition, BMW got the popular Range Rover brand and beat rival Mercedes-Benz in the race for a four-wheel-drive sport-utility vehicle. BMW Chief Executive Bernd Pischetsrieder believes Rover's price was approximately what BMW would have had to invest to design and produce a sport-utility vehicle from scratch. And since Rover also makes smaller and cheaper sedans, BMW was able to broaden its product range without diluting its luxury brand image.

**"A CANDY STORE."** Despite the strategic fit, Rover came with plenty of problems. BMW will need to make heavy capital expenditures to expand Rover's European distribution, now dangerously concentrated in Britain. The owners will also have to commit major resources to research and develop new models—about \$709 million in each of the next three years—because Rover had relied heavily on Japan's Nissan, its former partner, for engineering and design. In addition, Rover's subpar financials have dragged down those of BMW as a whole. Net profits on sales for 1995 are less than 2%, vs. 4% to 4.5% before the acquisition. Pischetsrieder insists the acquisition's costs have held no surprises, but he concedes: "We will need five years to get [Rover productivity] to the levels we need them to be." Frankfurt-based Schröder Münchmeyer Hengst Research expects Rover to hurt BMW profits for two to three more years, and rates BMW shares a sell.

Buying targets in the U.S. may take even longer to pay off. As the world's biggest economy with the added attractions of political stability and a favorable regulatory environment, the U.S. is "the candy store for the world," says Stephen B. Blum, national director for corporate finance at KPMG Peat Marwick. Of the 2,216 cross-border takeovers completed in the

first nine months of 1995, 427 involved an American target.

But as the Bumble Bee and Firestone examples demonstrate, the risks are high and range beyond mere cultural pitfalls. Foreign acquirers, for instance, on balance pay most twice as much as a domestic buyer would. According to KPMG, the average price paid by a foreign acquirer for a U.S. target in the first nine months of 1995 was \$78 million vs. a global average of \$39 million. Why the bonus? Says Blum: "\$10 million or \$20 million buys you a big chunk of the market in most other countries. In the U.S., it won't even buy you visibility."

Paradoxically, the weak dollar hasn't made U.S. acquisitions any cheaper. Instead, says David J. Ravenscraft, finance professor at the University of North Carolina's Kenan-Flagler Business School, buyers whose national currency is strong are often overbid because they feel flush. Besides their tendency to overpay, foreign acquirers don't do a good job of turning their targets' losses into profits, at least in the short term. Ravenscraft and fellow economist William F. Long, president of Business Performance Research Associates in Bethesda,

Md., carried out a pilot study of 88 American companies acquired by foreign buyers between 1977 and 1991. The results showed that in most cases, the new management failed to improve the target company's operating performance a year after the acquisition. Ravenscraft also cites the "hubris effect"—when foreign CEOs pay too much for U.S. companies for prestige instead of strategic or financial reasons. The most glaring examples are the Japanese, who have lost \$320 billion buying U.S. trophy properties since 1986, according to Nomura Research Co. They have since bailed out of money-losing U.S. assets from Rockefeller Center to MCA to fast-food chain Arby's.

American CEOs are subject to hubris, too. Former Chrysler Chairman Lee A. Iacocca bought stakes in Italian sports carmakers Lamborghini and Maserati in the mid-1980s largely out of self-indulgence. The acquisitions had virtually no business rationale, and Chrysler unloaded them in the early 1990s. Ford Motor Co.'s \$2.5 billion

acquisition of Jaguar Ltd. in 1989, when the British company was bleeding cash, still has many analysts shaking their heads. The auto maker has had to spend an additional \$1 billion improving Jaguar's notoriously poor quality and expanding facilities in Britain. Not until 1994 did Jaguar begin to turn out a small profit, and Ford is still nowhere near recovering its investment.

The high failure rate for cross-border acquisitions does seem to be deterring buyers. In fact, international deals in the first half of 1995 jumped 6% by number, to 2,778, and 25% in value, to \$111 billion over first-half 1994, according to KPMG. But unless companies figure out a less expensive way to do global, the disappointments are likely to continue.

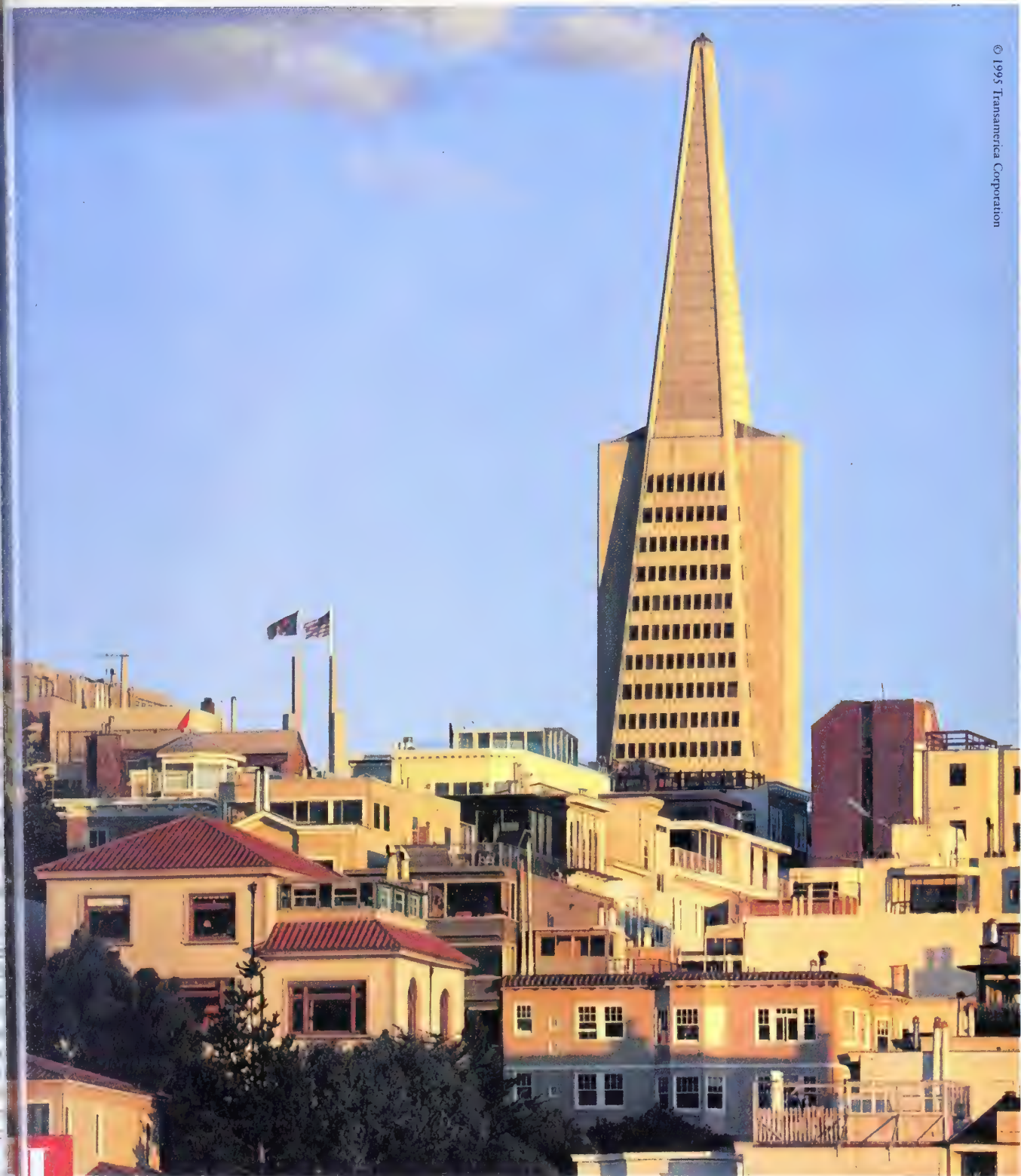
*By Joan Warner in New York, with John Templeman in Bonn, Robert Horn in Bangkok, and bureau reports*

## Pitfalls of Foreign Buying

- Foreign acquirers usually pay more for targets than a domestic buyer would, often with inflated hopes of future synergies
- Differences of language and culture aggravate integration of two management teams
- Misperceptions about the target's home market can lead to marketing gaffes
- Vertical integration is much harder in cross-border deals than intra-country deals
- Employees tend to be even more frightened of new management if bosses are from another country

DATA: BUSINESS WEEK





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# COMPANIES THAT LIVE ALONE —AND LIKE IT

From Wal-Mart to Cabletron, those who resist the urge to merge can still end up winning

**W**ith merger mania raging unabated, today's conventional wisdom is that if you're sitting out this merger boom, you'll be left behind in the ruthless, competitive race to grow bigger and bigger. But look behind the headlines, and you'll find many go-it-alone companies are doing just fine. Corporations that eschew the urge to merge often show that the lonely road can lead to big returns. By sticking to one's knitting and resisting the lure of diversification—even into related lines of business—many companies have been able to best their competitors, from Wal-Mart outperforming Kmart to Coke beating Pepsi. Coca-Cola Co.'s chief financial officer, James E. Chestnut, extols the virtues of selling beverages, period. "The fact that we've focused on one business brings efficiency to our organization."

Take top nonacquirer Andrew Corp. in Orland Park, Ill. (table). Andrew, which makes antennas and transmission lines for telecommunications systems, has seen earnings grow 19% a year for the past five years as revenue jumped from \$366 million to \$558 million, says CEO Floyd L. English. "We're staying away from a megamerger.... We're better off putting our resources to work internally. All our real growth and development has occurred internally." New businesses and products that were generated from within amounted to more than \$100 million of the revenue added since 1993, the company says. And while Andrew has made small acquisitions to diversify product offerings, it has achieved strong results without big mergers. "It's tempting sometimes to grow that way, rather than do it internally, but I think that's shortsighted," says Chief Financial Officer Charles R. Nichola. **HARD LESSON.** Wal-Mart Stores Inc.'s blockbuster success has been achieved in part through a strategy of only very selective purchasing in its core business. The \$1 billion it spent in the past two years for 122 Woolco stores in Canada and about 100

PACE Membership Warehouse stores—which it bought from Kmart Corp.—was justified by the acquisitions' real estate value, not operating expertise, says J.J. Fitzsimmons, Wal-Mart's finance vice-president. Buying assets rather than tire businesses has occasionally been complemented by deals aimed at vertical integration. In 1990, Wal-Mart bought food distributor McLane Co. to give it grocery expertise. As Fitzsimmons puts it, these strategic moves help, but the company is not "be-

## FLOYD ENGLISH

Andrew Corp.

"We're staying away from a megamerger. All our real growth ... has occurred internally."

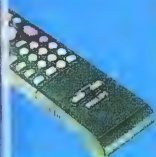


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# PHILIPS



# By sticking to its core businesses, Coke wiped out Pepsi's lead in East Europe, and it's far ahead in Latin America

forced to go to the acquisition market for growth."

That's a lesson discount-store giant Kmart learned the hard way. With Wal-Mart nipping at its heels in the early 1990s, Kmart gobbled up several specialty store chains. This heavy bet on diversification was quickly doomed, and Kmart was forced to sell off divisions in 1994.

In managed health care, fast-growing U.S. Healthcare Inc. bucked the megamerger trend by replicating its homegrown system in all of its regional markets. In the past 18 months, it has built health maintenance organizations from the ground up in Georgia, Virginia, Rhode Island, and central Pennsylvania. This year 314,000 new members have signed up, helping the company, based in Blue Bell, Pa., combat industrywide competition. "The only way you can assure the quality and consistency of that model is to build it from scratch your own way," says James H. Dickerson Jr., CFO at U.S. Healthcare.

For companies with cash to spend, acquisitions can be irresistible, especially if stockholders are antsy about maximizing returns. Just ask

Craig R. Benson, chairman of computer-networking success

## Special Report

Cabletron Systems Inc., based in Rochester, N.H. Most of Benson's competitors have been on a buying frenzy, leaving investors wondering why Cabletron, which averages a tidy 28% annual return on equity, isn't following suit. But Benson believes that keeping Cabletron's technology pure gives him an advantage in servicing clients. "The larger multinationals we sell to want the steering wheel in the same place and the gas pedal on the floor," says Benson. "What you find from cobble-together companies is the steering wheel changes sides and the gas pedal winds up in the backseat when their next product comes out." Cabletron recently traded at \$68 a share, just a shade off its 52-week high.

**SODA POP WARS.** But keeping new ideas constantly percolating isn't easy. At Motorola Inc., based in Schaumburg, Ill., the founding Galvin family has fostered an environment that encourages staff to pursue new ventures. The \$22 billion wireless-communications and semiconductor specialist spent \$1.8 billion on research and development alone last year. The R&D push continually spawns proprietary technologies, and that greatly reduces the need to go outside the company to fuel its growth. "Acquiring and merging is not in our history," says President Christopher B. Galvin. "We learn for ourselves and see what we can create."

When Motorola does work with other companies to move into new areas, it's usually through a lower-risk, lower-cost partnership. Currently, Motorola is paired with DSC Communications Corp., a Plano (Tex.) firm that makes switches for routing calls, in a bid to create the next generation of switches. If the technology works, Motorola gets to participate in a new market. If it fails, the company's losses will be minimal.

Even in an industry as simple as soda pop, internal investment can be the growth ticket. Under Chairman and CEO Roberto C. Goizueta, who took over in 1981, Coca-Cola has made only one significant non-

beverage acquisition: Columbia Pictures, which was sold to Sony Corp. in 1989. Since then, Coke has focused on growth in its core businesses, backed by aggressive investment in new markets and, recently, a sizable stock repurchase program.

That strategy has paid off handsomely for investors, with the stock rising elevenfold in the past decade, a 27% compound annual growth rate. International markets provide 80% of the company's operating earnings, and Coke has invested heavily in Eastern Europe and South America. When the Soviet bloc crumbled, the Atlanta-based bottler immediately

earmarked \$1.5 billion for investment in that region, including \$450 million for eastern Germany. Coke typically invests in local bottlers and concentrate makers. Then it begins to build roll distribution activities, advertising, retail space, and vending machines. "We've got all the possible opportunities we can handle in our core business," says CFO Chestnut.

More diversified risk: PepsiCo Inc. took an early lead in the region, generated by distribution deals with many former communist countries. But by late 1992, Coke had the market-share lead in every East European

## How Nonacquirers Do Better

- Stick to core capabilities
- Minimize capital risk by investing in existing operations or through joint ventures
- Reject growth for growth's sake
- Nurture innovation, which later provides avenues for internal expansion

DATA: BUSINESS WEEK

country, with Pepsi mounting a spirited counterattack. The duo is also battling over Latin America, with Coke far out in front. At a recent bottlers' convention, President Jack L. Stahl boasted that Coke has captured 90% of the domestic industry's volume growth this year.

Some of the companies that made BUSINESS WEEK's list

of top nonacquirers, such as Compaq Computer Corp. and Enron Oil & Gas Co., are businesses that have eschewed mergers in the last few years. Freeport-McMoRan Copper & Gold, which is No. 2 on the list, has invested \$2.5 billion in internal development since 1989. The energy industry tends to collaborate in partnerships rather than pursue mergers.

With a healthy economy helping to drive the merger trend, today's nonacquirers seem very much out of step. But if the economy slows, more companies may announce mergers, predicts University of Chicago finance professor Steven Kaplan. "Expansions like the one we're now tending to put companies in the spend mode. Recessions tend to put them in a digestive phase," he says. That may force today's merger partners to become tomorrow's masters of internal growth.

By Nanette Byrnes in Los Angeles with Paul C. Judge in Boston; Kevin Kelly in Chicago; David Greising in Atlanta and bureau reports

## The Top 10 Nonacquirers

|                      | MARKET-VALUE APPRECIATION VS. INDUSTRY INDEX |
|----------------------|----------------------------------------------|
| Andrew               | 1.28                                         |
| Freeport-McMoRan C&G | 1.27                                         |
| Cabletron Systems    | 1.27                                         |
| Micron Technology    | 1.23                                         |
| Applied Materials    | 1.23                                         |
| Lowe's               | 1.22                                         |
| Compaq Computer      | 1.21                                         |
| Hercules             | 1.19                                         |
| Enron Oil & Gas      | 1.18                                         |
| Engelhard            | 1.17                                         |

DATA: MERCER MANAGEMENT CONSULTING, SECURITIES DATA CO., S&P'S COMPUSTAT, BW

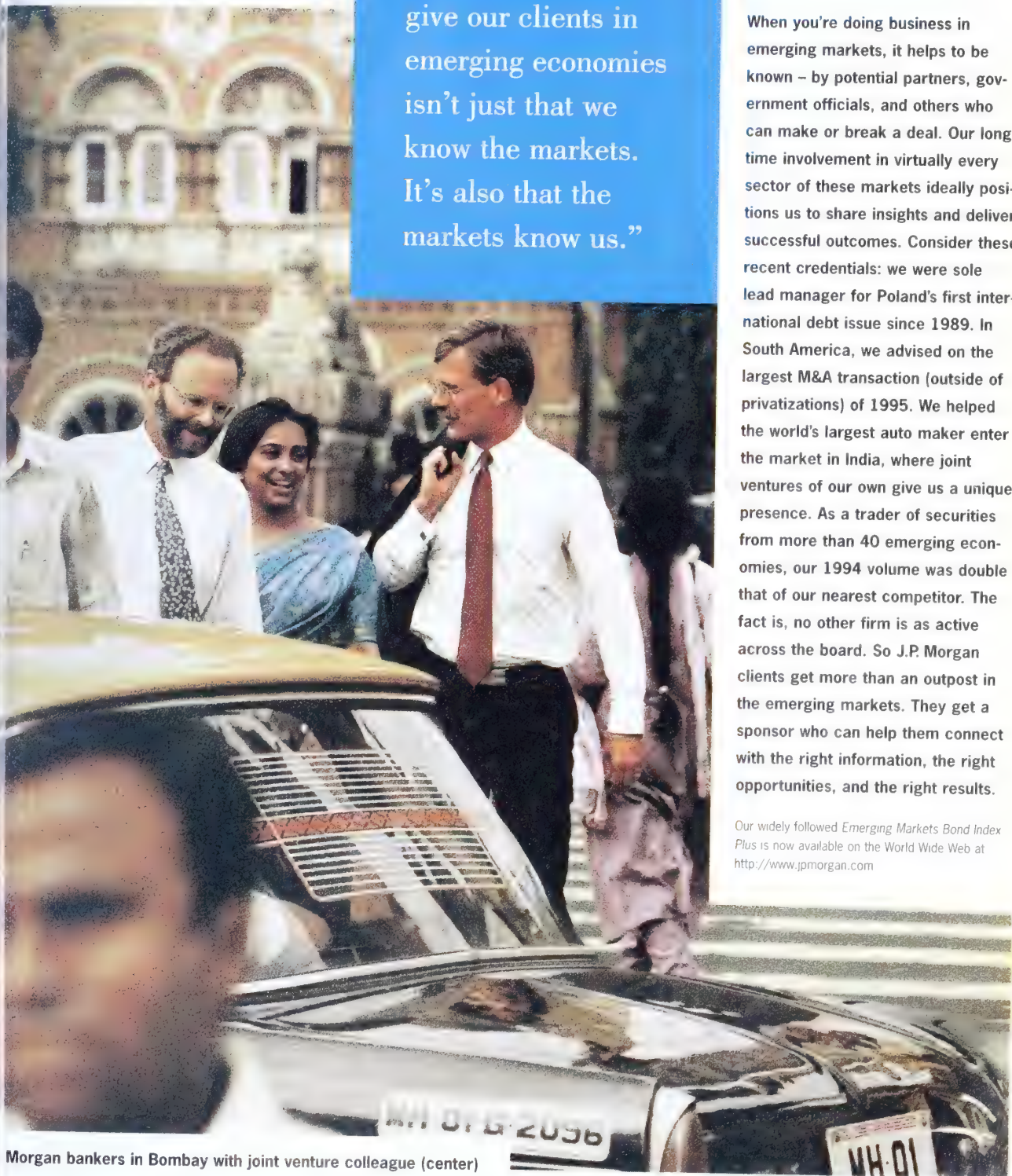


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## JPMorgan



BY GENE G. MARCIAL

## KEEPING AN EYE OUT FOR BAD RISKS

In the 1970s, Bob Olstein spelled bad news for many: His *Quality of Earnings Report* looked behind official numbers—and put a lot of stocks under a cloud. Now, Olstein is back, as a stock sleuth and president of Olstein & Associates. It aims mainly to spot risks before looking at upside potential, an uncommon approach to sizing up stocks.

Olstein's sleuthing prompts him to short shares of toymaker Mattel (MAT) and food-service chain Boston Chicken (BOST). He says they are burdened with debt and engage in aggressive account-

### OLSTEIN'S STOCK BETS

| Stock          | 1995 high | Oct. 17 price | Estimated value |
|----------------|-----------|---------------|-----------------|
| ETHAN ALLEN    | \$25%     | \$20%         | \$30            |
| FLEETWOOD      | 24 1/2    | 20            | 30              |
| RPM            | 21 1/2    | 19 1/2        | 29              |
| WET SEAL       | 6%        | 6 1/4         | 10              |
| MATTEL         | 30%       | 27 1/2        | 21              |
| BOSTON CHICKEN | 30        | 28 1/4        | 15              |

DATA: BLOOMBERG FINANCIAL MARKETS, OLSTEIN & ASSOCIATES

ing, so that "investors have unrealistic expectations of the earnings potential."

On the long side, he is snapping up furniture maker Ethan Allen (ETH), homebuilder Fleetwood Enterprises (FLE), industrial-coating maker RPM (RPOW), and Wet Seal (WTSLA), a retailer of moderately priced women's clothes. Aside from being cheap, some of these stocks are good buyout candidates, he says. Olstein's portfolio in the past 13 years, while at Smith Barney, had 23 stocks that were taken over.

Olstein's reputation as a no-nonsense stock-picker enabled him to raise \$100 million in two weeks for the Albany (N. Y.) Olstein Financial Alert Fund, which his firm manages. His forte is analyzing financial figures—without talking to management at all.

"We wanted to buy into Mattel, but upon closer examination we concluded that the best way to make money in Mattel was by shorting its stock," says Olstein. He notes that almost all of

Mattel's earnings of 41¢ a share in the first half of 1995 came from a lower allowance for "doubtful accounts," lower advertising as a percentage of sales, lower tax rates, and currency translations.

"These mainly nonrecurring factors suggest there was no earnings growth," he explains. He also notes that Mattel had \$48 million in negative cash flow in the first six months of 1995. And from June, 1994, to June, 1995, inventories leaped 40%, while sales grew only 17%. Olstein is also concerned about the debt jump—from \$440 million to \$630 million in about two years. A Mattel spokesman says Olstein is "totally off base: Our business has been very strong, and he has failed to consider the seasonality of our business."

Boston Chicken is another example, says Olstein, of a company reporting earnings that aren't from "real" operations—in this case, from franchisees' fees and royalty payments. Melissa Marsden, Boston Chicken's investor relations officer, insists that earnings are real because the company provides significant support and services to the franchisees. "We're making great progress at the store level," she adds.



GO FIGURE: Olstein sticks to numbers

## A 'NEAR-PERFECT' PHONE OUTFIT

If Tony Hitschler could buy just one stock, he would pick BCE (BCE), whose subsidiary, Bell Canada, provides telecommunication service to 70% of Canadians. "It's a near-perfect company, and its stock has everything we're looking for," says Hitschler, president of Brandywine Asset Management. "I wish all the stocks in our [\$4 billion] portfolio were like BCE."

What's so alluring about BCE? The company, which also owns 52% of Northern Telecom, a big maker of phone gear, is way undervalued, notes Hitschler, based on such benchmarks as price-earnings ratio, price-to-cash-flow, and price-to-book-value.

Now at 33, the shares have a break-up value of 55, he figures. According to his calculations, Bell Canada alone is worth 24 a share, and Northern Tele-

com more than 16. BCE also has mobile communications operations and is engaged in natural-gas transportation and financial services. The stock is "misvalued" in the sense that most investors consider it a dividend play because of its 6% yield, says Hitschler. Price-to-cash-flow is a more appropriate measure for this technically sophisticated company, he thinks. Based on this measure, the price should be 50

## HOP ON THIS FAST FREIGHT

Conrail (CRR) may be next in line for the rails' buyout blitz. Railroads have been busy crossing tracks toward mergers. The most recent marriage—Burlington Northern Railroad and Santa Fe Pacific—created the nation's largest system. In May, Union Pacific merged with Chicago & North Western. No one is betting that Conrail and Norfolk Southern will opt to merge, after talking about—and abandoning—the idea 1½ years ago.

Some believe the two companies have held talks about a merger or outright takeover of Conrail, which operates the Northeast and Midwest. Norfolk operates in the Southeast and Midwest.

Speculation about a merger may account for the continued climb of Conrail shares, currently trading near the high of 72. One New York strategist believes Norfolk will bid 85 or 90 for Conrail. Conrail declined comment about any merger—insisting its strategic plan was to stay independent. Norfolk also declined to comment.

Analysts view a Conrail-Norfolk match as a perfect fit: Eliminating parallel routes would bring huge cost savings. Conrail is regarded as one of the best managed in the country. Although the stock has risen fast partly on buyout speculation, "we're still bullish on Conrail because of its fundamentals," says Burton Strauss Jr., an analyst at Lehman Brothers. He figures it will make \$4.65 this year and \$5.50 in 1996, versus last year's \$3.90.

### CONRAIL PICKS UP SPEED



DATA: BLOOMBERG FINANCIAL MARKETS





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# THE VIEW FROM IBM

Lou Gerstner does have a vision: Network-centric computing. Here's an inside look at Big Blue's blueprint

In July, it looked as if Louis V. Gerstner Jr. had earned a well-deserved rest after two years at the helm of IBM. The giant was no longer listing, and cash was pouring in. On July 5, Big Blue closed the \$3.5 billion deal to buy Lotus Development Corp., and the stock price was about double what it had been at the start of Gerstner's reign—making the CEO's options worth approximately \$32.5 million. In August, Gerstner even took time for a five-day family vacation in Italy—sandwiched between calls on European customers.

Now, summer has turned to fall. And the outlook for IBM has turned from euphoric to cautious. On Oct. 11, Lotus chief Jim P. Manzi resigned, raising concerns over how the company is managing the strategically important merger. Manzi's departure is just the latest in a string of developments that are making this a tough season for Big Blue's CEO. In September, the company announced delays of two key products, and Jerome B. York, architect of Gerstner's cost-cutting crusade, quit. Both events raised questions about IBM's earnings momentum.

On Oct. 17, the company reported third-quarter earnings of \$1.3 billion—excluding a one-time charge of \$1.8 billion for the Lotus purchase—on revenue of \$16.8 billion. The net was 6% below earlier projections. IBM's stock slid from a high of 114% in August, as some analysts cut earnings estimates for the year, and now trades in the mid-90s. As York told reporters when he left to join Kirk Kerkorian's Tracinda Corp., the cutbacks that helped boost 1994 earnings to nearly \$3 billion—after losses of \$16 billion over the previous three years—are

largely over. "Management's attention is focused heavily on the revenue side of the equation," he said.

In other words, Job One is finding a long-term growth strategy for the world's largest computer company, a mammoth organization that has grown at only a 3.3% annual rate for the past decade. What Gerstner needs—and is quietly pulling together—is a plan to seize what may be IBM's greatest opportunity: to become a leader in the dawning world of networked computing and electronic commerce. In this new wave of computing, communications rather than computation is the key. It involves everything from multimedia PCs to the vastness of the Internet.

"One of the great things about this industry is that every decade or so, you get a chance to redefine the playing field," Gerstner told BUSINESS WEEK in an exclusive interview. "We're in that phase of definition right now, and winners or losers are going to emerge from it."

The driving force is the arrival of low-cost digital networks that are spreading everywhere. Using high-speed fiber-optic cables and lightning-fast switches, digital networks will carry a whole new host of communications-based applications, such as teleradiology (transmission of X-ray images), distance-learning in the education market, or electronic transactions in business.

"Network-centric computing," as Gerstner calls it, is remaking the computer business the way the low-cost power of the microprocessor overwhelmed the mainframes and minicomputers

of the 1980s. "Communications will change IBM more than even semiconductors have," predicts Howard Anderson, president of market researcher Yankee Group Inc.

It's an opportunity Gerstner says he knew he had to seize at the outset. But first he had more pressing chores, such as shoring up the balance sheet and restoring IBM's credibility with customers and investors. Also, he notes, there were problems getting some IBMers on board. "I sensed there were too many people inside IBM who wanted to fight the war we lost," he says.

**CLEAR SIGNAL.** The lost crusade, of course, was the battle for supremacy in personal computers. With the IBM PC, the computer giant had a winner. But it lost its position by ceding technical leadership to Intel and Microsoft and the market edge to Compaq Computer and a host of cloners. Now, Gerstner has sent a clear signal within IBM to refocus on the future. He has disbanded a unit that was trying to create an alternative to Intel-based PCs that would have used the IBM-Motorola-Apple Computer PowerPC chip. He also has ordered a retreat from the costly losing battle that pitted IBM's OS/2 against Microsoft's Windows in desktop computers. The new contest is in networked software, Gerstner says—which is why he is willing to pay billions to acquire Lotus and Notes "groupware" program (page 148).

The CEO still shies away from announcing a grand vision of IBM's future—after being lambasted for declaring early in his tenure that none was needed. But on a warm October morning, as he talks about the future of IBM and networked computing in a conference room next to his office, it's clear that he has one (page 152). Gerstner excitedly paints a picture of a 21st century business milieu in which networks become the lifeblood of corporations and the principle means of commerce. Eventually, he says, electronic commerce will extend to home shopping and other consumer transactions, too. Then, however, IBM may be reaching consumers with a network other than Prodigy Services Co., the long-struggling IBM-Sears Roebuck venture. "We are taking a hard look" at Prodigy, says Gerstner.

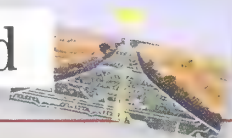
Gerstner's scenario hinges on some critical changes in I



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## What's Down The Road



“One of the great things about this industry is that every decade or so, you get a chance to redefine the playing field. We're in that phase of redefinition right now”

— LOU GERSTNER, IBM



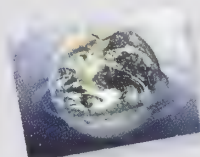
### Network Applications



An incubator for services and software designed to operate across a variety of networks, including IBM's own network, Prodigy, and the Internet. The 200-person unit oversees nascent efforts in e-commerce, collaborative computing, content services, and interactive TV.

**RIVALS: ORACLE, MICROSOFT, AT&T, WELLS FARGO, BARRICK**

### Global Networking



With net connections in more than 100 countries and 850 cities, IBM is one of the biggest companies in networking. The heavy-duty corporate net serves 25,000 customers and doubles as the backbone for Prodigy. The network also delivers Notes-based applications and Internet access.

**RIVALS: AT&T, MCI, EDS, BRITISH TELECOM**

### The Internet



The business of helping customers design and maintain Internet sites is small but growing. Customers from the Australian Chamber Orchestra to the Professional Baseball Organization of Japan have Internet home pages designed by IBM, which provides consulting services and security software.

**RIVALS: SUN MICROSYSTEMS, AT&T, MCI, DIGITAL EQUIPMENT**

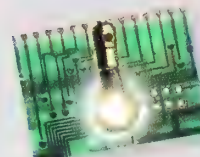
### Industry Sales Units



IBM now reaches 80% of its customers through a sales force that is divided into 13 industry-specific units in such areas as financial services, travel, health care, utilities, and insurance. Such industry expertise should help the industry giant sell its products and services.

**RIVALS: EDS, ANDERSEN CONSULTING**

### Information Services



One of IBM's fastest-growing units is Integrated Systems Solutions, which handles mega-outsourcing deals for the company's biggest clients. With its order backlog worth \$30 billion, the organization is growing by more than 33% a year. Latest hot segment: Managing PCs and networks.

**RIVALS: AT&T, EDS, COMPUTER SCIENCES**



products and the company itself. If he can't get his troops to act quickly on his plan—and prove that IBM really has its networking act together—the computer giant's claim to leadership in the new era will remain wishful thinking. Competitors, naturally, say Big Blue will stay mired in the pre-network past. They point out, for example, that it has already missed hot markets for local-area networks (LANs) and related gear. "To say that IBM has seen the light—give me a break!" says Scott G. McNealy, CEO of Sun Microsystems Inc.. "We say to customers, IBM, DEC, and HP understand where you've been. We understand where you want to go with the Net."

What is IBM's network vision? Mainly, it's about bringing the company's traditional customers to network nirvana. "What is every major institution in the world focusing on?" asks Gerstner. "It's called reengineering. It's called getting competitive. It's called reducing cycle time and cost, flattening organizations, increasing customer responsiveness. All of these require a collaboration with the customer and with suppliers, and with vendors." All of these efforts, in short, depend on networking.

What Gerstner is doing—though so quietly that it's easy to overlook—is arraying resources from all over his empire for an assault on the wired

## Cover Story

world. And guess what? IBM has a lot to fight with. It has the world's largest private data network, an army of consultants and technicians to create custom networks and software for any type of business, and it even has some cutting-edge technology such as high-speed communications switches and software to enforce copyright protection on the Information Highway. Best of all, even IBM's biggest detractors concede that the company has enduring relationships with big corporate customers that are eager to squeeze time, cost, and inefficiency out of their operations.

IBM also has lots of competition. Everybody from AT&T and its long-distance rivals to all of the Baby Bells to Electronic Data Systems, Sun, Intel, and Microsoft to Oracle are racing into position. But Gerstner argues that his company has a nearly unique set of skills with which to bring corpora-

### MAKING IT EASY

An IBM mainframe tells DowBrands how many of each product to send to stores—and when. P&G uses the service, too. A system developed by Walgreen lets doctors send prescriptions to pharmacies electronically. Pharmacies will pay IBM a fee per Rx



tions painlessly into networked computing. As the world gets wired, access to computing power and applications becomes easier, but the complexity of building these systems—especially ones that operate around the world—so "IBM is one of the few companies that has the infrastructure to provide information systems on a global scale," says Gerstner. Ross, a co-founder of Change Lab International Inc., a Stamford (Conn.) consultant.

**BIG IS BEAUTIFUL.** Broadly, the plan is to use the computer giant's global reach, its expertise in dozens of technologies, and its knowledge of how major customers conduct their businesses to offer all sorts of computing resources across the world—either private or public ones. The network becomes an information-technology resource that customers can use outright or rent as needed. Someday, they might not even need a computer staff or data center. "People will just run into the wall and not care where the computer is," says Harry Wallaesa, chief information officer for Campbell Soup Co., a major IBM customer.

In the wired future, says Gerstner, companies will be able to buy computing power and applications software the way they buy electric service. "They will rent them on a per-use basis because they will be resident in the network," he predicts Gerstner. "Think about the implications of a world in which the application is on the server—all applications

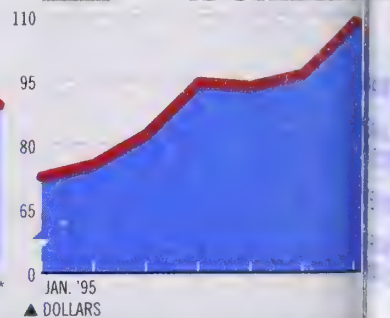
## Why IBM Needs a Growth Strategy

DATA: SALOMON BROTHERS INC., INDUSTRY ESTIMATES

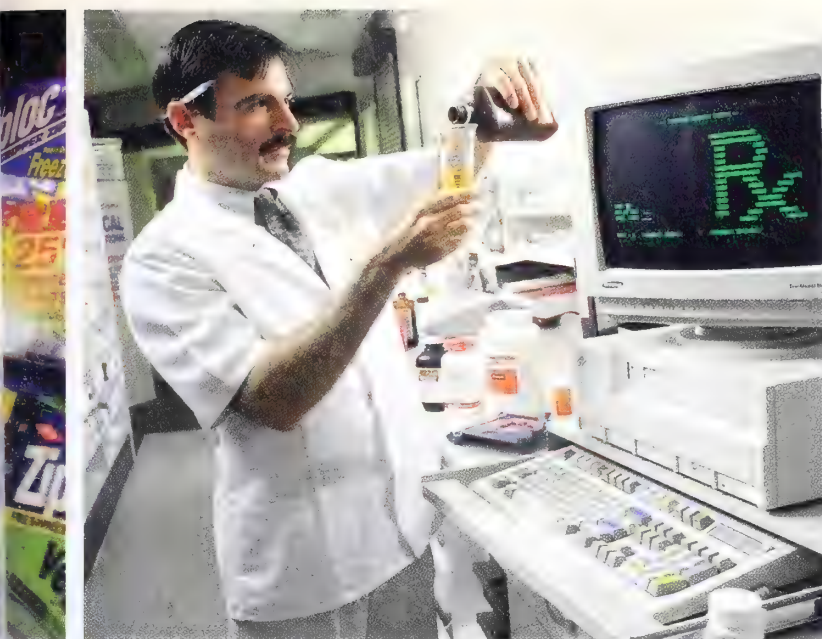
**EARNINGS ARE ON THE RISE...**



**...BUT THE STOCK IS STALLING**







efore that world takes shape, the 53-year-old CEO has a o accomplish. An important first step: convince program—in corporations and at software companies—to write ications for IBM networks. "They have to redefine where ications are developed, from the desktop to the net-," says industry consultant Marc Schulman.

at's where Notes can play a critical role. It's already a seller among the large corporations that use IBM main- es. On Oct. 3, IBM announced Notes Public Networks, an ement with 11 communications companies—including sh Telecom, CompuServe, and Nippon Telegraph & Tele- e—to carry the program on their networks. That will e it easier to experiment with the groupware setup. immediately lower the barriers for acceptance of Notes," Fernand B. Sarrat, an IBM general manager for network ces. "Customers can go directly into a Notes service."

other way Gerstner is getting ready for the network- ible future is by building up Big Blue's outsourcing and ms-integration businesses. Outsourcing involves taking a company's data processing operations and then selling computing service or simply running the operation for a annual fee. Campbell Soup, for instance, recently signed 0 million deal for IBM to run its data center, network, and desktop computers for 10 years. In the networked l, outsourcing will become more common and more so-

phisticated. IBM and other companies will design, create, and install "solutions" to business problems that customers can use by tapping into the Net.

**HONOR CODE.** Consider what's happening at DowBrands Inc. The maker of Ziplock bags and Fantastik is using an IBM network "solution" that it hopes will put it on the cutting edge of logistics. Every day, an IBM mainframe sitting in Rochester, N. Y., gets electronic updates from Dow's retailers on their inventories. The data are analyzed using Dow's production schedules, records of the retailers' past buying patterns, and other factors. When Dow taps in, the system can tell the company how much of each product to send to each retailer and when. Dow doesn't own the software or the computers. And it shares the service with rivals such as Procter & Gamble Co., which developed the software. Dow and the others trust IBM to keep the information secure and confidential, and each pays a monthly usage fee based on its volume of transactions.

Another convert to IBM's new pay-as-you-go system is Walgreen Co. The drugstore chain is testing a new system that allows doctors to electronically send prescriptions to pharmacies. The system saves time for doctors and drugstores, prevents pharmacists from misreading handwritten prescriptions, and can flag potential medical problems. Walgreen developed the software but sold it to IBM because it feared that doctors and other chains would balk at using a system run by one retailer. Now, other chains, such as Eckerd Corp., are trying it. Doctors get the service for free. Walgreen and other pharmacies pay a fee for each prescription.

Sure, it's penny-ante stuff now. But a few pennies here and there will add up. Walgreen and other drugstores will pay IBM from 12¢ to 18¢ per prescription. In the U.S., 2 billion prescriptions are filled every year, and IBM already has 25% of the nation's drugstores testing the system. What's more, once the system is in the doctor's office, other services can be sold—from patient billing to downloads of the latest articles from medical journals.

For customers, the savings are alluring. They don't have to buy multimillion-dollar mainframes, hire computer operators, or sink capital into data centers. "The economies involved in doing this are going to be significantly better than if you own your own computer," says Frank X. Dzubeck, president of market re-

## OVERALL, CORE BUSINESSES ARE GROWING SLOWLY...

|              | REVENUES<br>BILLIONS | 1995 GROWTH<br>ESTIMATE |                     | REVENUES<br>BILLIONS | 1995 GROWTH<br>ESTIMATE |
|--------------|----------------------|-------------------------|---------------------|----------------------|-------------------------|
| ARE          | \$12.3               | 9%                      | MINICOMPUTERS       | \$4.2                | 14%                     |
| NAL<br>JTERS | 10.6                 | 13                      | RENTAL/<br>FINANCE  | 3.4                  | -1                      |
| ENANCE       | 7.4                  | 3                       | STORAGE<br>PRODUCTS | 3.2                  | -9                      |
| RAME<br>VARE | 6.2                  | 0                       | PRINTERS            | 0.9                  | 3                       |



## ...WHILE A FEW NEW EFFORTS SHOW PROMISE

|                         | REVENUES<br>BILLIONS | 1995 GROWTH<br>ESTIMATE |
|-------------------------|----------------------|-------------------------|
| SERVICES                | \$12.6               | 33%                     |
| COMPONENT<br>TECHNOLOGY | 4.2                  | 28                      |
| WORKSTATIONS            | 3.1                  | 51                      |

DATA: SALOMON BROTHERS INC., INDUSTRY ESTIMATES



# Future IBM customers may do without a computer staff They'll just buy what they need, the way they buy electricity

searcher Communications Network Architects Inc. Campbell Soup expects to save \$200 million over the life of its deal.

IBM is already enjoying a boom in computer services. With \$9.5 billion in revenues last year, IBM's outsourcing and systems integration business was second only to \$10 billion Electronic Data Systems Corp. In the first half of this year, IBM's business grew at a 33% annual rate, while EDS is expected to grow 20% in 1995. On Oct. 11, Nynex Corp. picked IBM to help build a multimedia network and applications programs to sell on it. It's good business for Big Blue, says Ward MacKenzie, vice-president for Nynex Business Network Solutions. "In just my business market, we have access to 1 million customers," he says.

In addition to putting a new leg on the services business, Gerstner counts on networking to bolster other IBM divisions. Even as customers switch to buying computing across the network, they will still need new desktop computers, network servers, even mainframes in their various offices and plants. The IBM CEO is convinced this will "reenergize" the market for very powerful servers—which is how mainframe-class systems are referred to in the networked era. Conventional mainframes as well as IBM's new SP-2 parallel computers can

act as transaction and database managers and keep secure huge quantities

of data and applications software. First, Gerstner concedes, such machines "have to be modernized and adapted very significantly."

IBM may require an image overhaul, too. Rebuilding around a network-centric strategy is "exactly what they must do," says Robert Djurdjevic, president of consultant Annex Research Inc. "But that's not my perception of what they are doing." Gerstner acknowledges the image problem and says his style may be partly to blame. "I have this quaint view that you perform and then you talk about it," he says. "That's not the modus operandi of this industry—you talk about something, then you perform."

On Nov. 13, Gerstner will have his chance to talk. That's when he'll be the keynote speaker at Comdex, the computer industry's largest trade show. He'll use the speech to describe how network-centric computing is going to drive the next phase of growth for the computer industry and its customers. **REINING IN.** Meanwhile, he continues to put key pieces of his plan in place. Frustrated by slow progress in getting various IBM units to collaborate on network strategies, Gerstner is pushing executives to pull together technology and marketing efforts from various divisions. He has already pulled more than 100 far-flung network operations—including Advantis, the huge U.S. data and voice network jointly owned by IBM and Sears, Roebuck & Co.—into a single operation, called IBM Global Network. "Customers want to operate globally," says John M. Whiteside, who was recruited from MCI Communications Corp. to run IBM's network operation a year ago. "To do that, they need a single network." IBM Global Network is now one of the biggest Internet access providers, with more than 100,000 subscribers.

Gerstner is also making sure IBM develops content for the wired world. The Networked Application Services Div., headed by Sarraf, has \$100 million to develop systems for electronic publishing, online catalogs, and videoconferencing that can be delivered over the Global Network, the Internet, or Prod-

igy. One new service, called infoMarket, uses a technique called "cryptolope" that lets publishers offer their wares in cyberspace without getting ripped off. If a consumer sees information listed online, he or she clicks a button, sending a message directly to the publisher, who then tells the client how much to pay to unlock the encrypted file. IBM, along with AT&T, Xerox, and a host of startups, is also working on methods for enforcing copyrights online.

If all of these efforts fail to make IBM a leader in network



computing, what then? Then, the current concerns for IBM's growth potential could quickly turn to alarm as investors try to figure out where future earnings will come from. Until this summer, it looked as though Gerstner was on track to restore IBM's growth to the overall industry rate, around 10%, by 1996. He counted on winning back market share in key segments such as PCs and software. But IBM's PC business, though rebounding, is growing at below the industry rate, and software revenues are growing modestly. The service unit is booming, but mainframes—still the company's most profitable business—are flat. Because of delays in new mainframes and mainframe disk-storage products, nearly \$1 billion in revenue expected in the third quarter is being pushed into the fourth quarter. Gerstner also plans to take a \$800 million charge in the fourth quarter to cover another spurt of cost-cutting.

And next year could be tricky. Should the U.S. economy

## Cover Story

### WIDE REACH

Network services exec Sarraf has \$100 million to develop systems for electronic publishing, online catalogs, and videoconferencing

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**Will the cars on the drawing board today meet consumer demands of tomorrow? That's the question facing J.D. Power and Associates. The answers are coming from the SAS System.**

"We produce a monthly forecast of car and truck sales for about 300 different vehicles," says Jon Rosenthal, Manager of Automotive Forecasting for J.D. Power and Associates. "Each vehicle is forecasted by month for five years beyond the current year. Right now I'm forecasting through the year 2000."

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"The SAS System is the fuel behind those forecasts...our software of choice for analyzing sales, economic, and auto industry data and then reporting what we've learned," adds Rosenthal. "Before the SAS System, much of the forecasting was done by hand. To make our forecasts credible, we had to have a credible system. One that made it easy to build applications and put them to work across our computing environments. We've got minis, Macs, desktop publishing, and a lot of spreadsheets. The SAS System fits the way we do business."

## ***The Bottom Line is Information***

Now that the forecasting model is up and running, Rosenthal and his staff are using the SAS System to build an interactive database. "The Power Information Network will allow an auto dealer or manufacturer to go online and get market information," Rosenthal explains. "When released,

subscribers will be able to select from a long menu of reports and data. The versatility of the SAS System is crucial in developing the reports."

"The bottom line is this: applications are being developed with the SAS System that will deliver the most up-to-date information to those who make decisions for the automotive industry," says Rosenthal. "If manufacturers and dealers can get their hands on accurate market information and predictions, they have a much better chance of meeting customers' needs down the road."

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slow and Big Blue's European business remain flat, some forecasters believe Gerstner may have to lower his sights to 6% or 7% growth for 1996—about what analysts expect for this year. That means IBM would continue losing share in key markets. Says a former senior IBM executive: "The more the company doesn't grow at the industry pace, the more it's behind the times."

## Cover Story

Launching a successful network-computing strategy is no quick fix. It's bound to be a long and frustrating effort, full of false starts. Some IBM network projects already have fallen behind schedule or fallen apart. Intelligent Communications Services, which was hyped as a way to bring together mail from multiple electronic and voice mailboxes, was supposed to be ready by the end of 1994. But the group de-

veloping it failed to get a prototype to work and was quietly disbanded.

There's little time for such missteps, and Gerstner knows it. The Internet is sweeping the computing landscape, and if IBM isn't careful, it could overwhelm Big Blue's networked forts. "There's no question that the speed with which the Internet has emerged has caught all industries related to the technology by surprise," Gerstner concedes. Like other companies, IBM has seized on the Internet's World Wide Web as a nifty new way to communicate with customers, and it's a business, though small, in helping customers use the Internet. **PARALLEL COMPUTING.** But the Web could also undo Gerstner's plans for Lotus. The Web setup can already perform some basic publishing and info-sharing tasks that companies buy Notes for. And in September, Web superstar startup Netscape Communications Corp. acquired Collabra

## CAN IBM KEEP LOTUS BLOOMING?

**W**hen IBM bought Lotus Development Corp., it placed a fat bet on networking. The computer maker spent \$3.5 billion and is expected to pay hundreds of millions more for the cost of goodwill over the next three years. This big pile of chips is mainly riding on Notes, a \$300 million-a-year business and the leader in "groupware," because it's the future. It can become, says IBM Chief Executive Louis V. Gerstner Jr., the glue to link workers, partners, and customers in virtual corporations—perhaps making it more important than any underlying Microsoft Corp. operating system. Says Morgan Stanley & Co. analyst Steven M. Milunovich: "Losing to Windows 95 isn't so important if Notes wins."

Will IBM be able to fulfill the Notes promise? All eyes are on Gerstner. His first crisis came on Oct. 11, with the surprise resignation of Lotus CEO Jim P. Manzi, who had asked to be put in charge of big chunks of IBM's software empire. Gerstner let Manzi go but was quick to reassure Lotus employees that the subsidiary, based in Cambridge, Mass., would not be forced into an IBM mold. He named two respected Lotus execs to a new Office of the President and secured the services of Notes developer Raymond Ozzie. IBM will also send many of its software salespeople to work for Lotus.

Gerstner can't risk letting organizational or morale problems slow the momentum Notes has built up. Already, corporations are asking whether

they might not get the same capabilities Notes gives them for a lot less by using the Internet's World Wide Web. "It's probably the single largest issue looming over Notes' future," says Eric C. Dean, a partner at Arthur Andersen Worldwide Organization, which uses Notes to connect 50,000 consultants and auditors around the world. Netscape Communications Corp., the hot Web startup,

### MEDITATING ON UNITY

Big Blue ran this ad right after it bought Lotus. Now, Manzi's exit has IBM moving quickly to bolster ties between the two companies



IBM and Lotus in spiritual harmony

took aim at Lotus with its Sept. 21 purchase of Collabra Software Inc., a low-end Notes competitor.

IBM recognizes that the Notes lead is perishable. "Increasing the number of Notes seats is our No. 1 priority," says John M. Thompson, IBM's software chief. He hopes to have Notes running on 20 million desktops by the end of 1997, from just 2 million today. That's ambi-

tious, but in the latest quarter, Notes sales jumped 300%, to 1.1 million copies.

Another thrust is to make Notes available over public data networks, so corporations can use Notes without building and operating their own networks. Phone giant AT&T launched its Network Notes service in September. On Oct. 3, seven more companies—including Japan's Nippon Telegraph & Telephone Corp. and Deutsche Telekom—announced Notes networks. IBM figures such networks could make up 30% of Notes "seats" in two years.

**WEB CONVERSIONS.** The job of building an IBM software strategy around

Notes is just beginning. IBM has started to adapt some of its workhorse programs, such as the DB2 mainframe database and MQ messaging software, to work smoothly with Notes. Notes 4.0, due around yearend, will expand the number of workers a Notes setup can accommodate, from around 5 to as many as 1,000.

There are efforts to reach Internet fans, too. A new package, InterNotes, lets companies convert Notes documents into the Web's HTML format. It also lets companies pull Web material into Notes. Version 4.0 will include "agents" for going out on the Net and automatically fetching information. Gerstner has given John Landry, Lotus's chief technologist, the job of forging a unified Internet strategy from the two companies' various efforts. That may be key to making the Lotus gamble pay off.

*By Amy Cortese in New York*

How could the builder get an injured carpenter back on the job?

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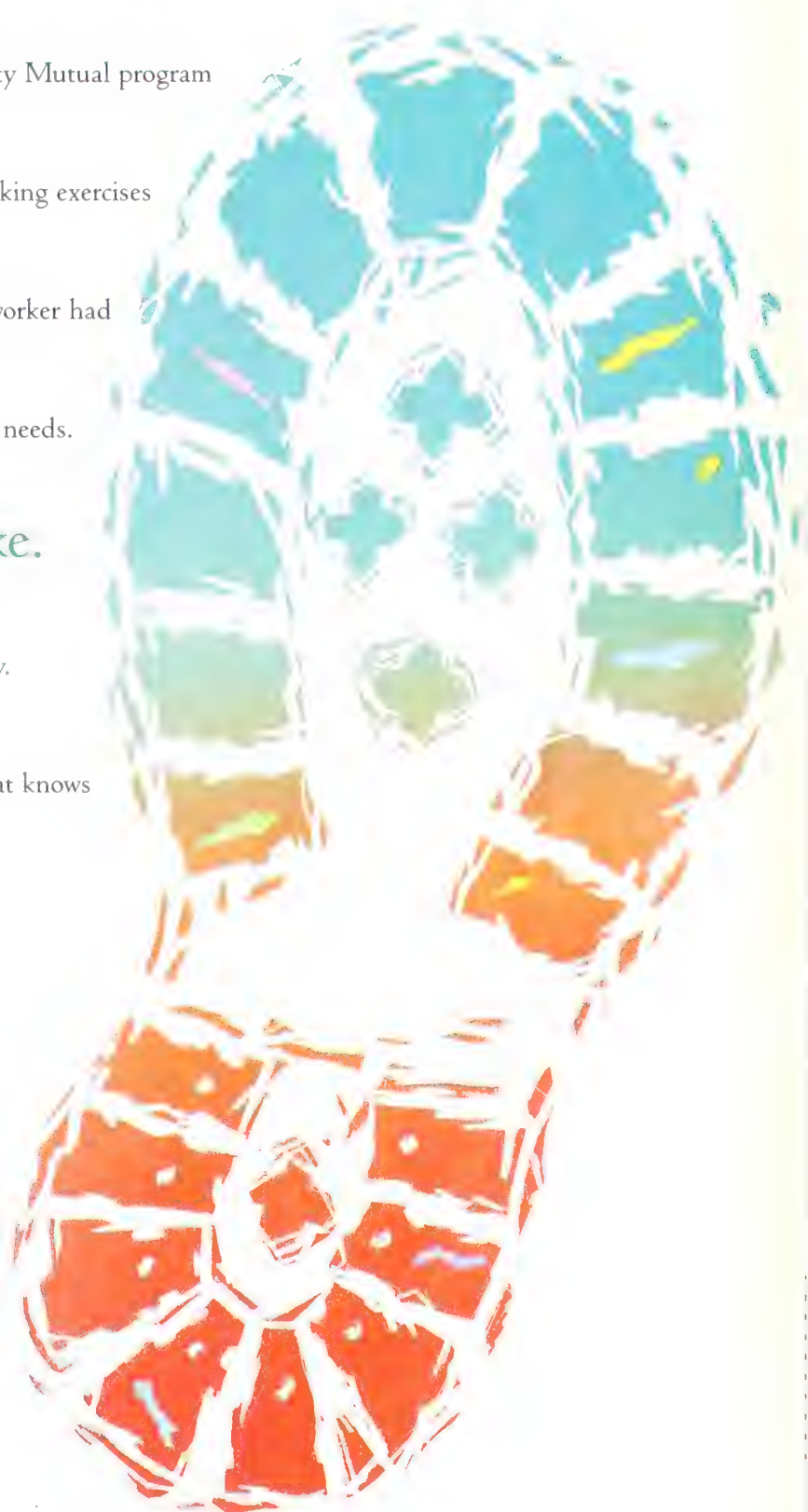
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software maker that competes with Lotus in groupware. "I think [IBM] bought Lotus Notes at the end of its life cycle—when everything is going Internet," says software magnate Lawrence J. Ellison, CEO of rival Oracle Corp. Just a year ago, Ellison himself considered acquiring Lotus. Now, he predicts: "Notes will be

## Cover Story

the Visicale of groupware"—referring to the once dominant PC spreadsheet that was killed off by Lotus 1-2-3.

Gerstner has no choice but to get IBM zeroed in on the networked future. If the IBM net replaces—or even augments—the mainframe as the key information technology

for big companies, IBM will retain "account control" and gain an advantage in selling a host of other products and services from PCs and network servers to huge collections of disk drives. "IBM is leveraging the network," says Jim Dowden, director of logistics for DowBrands. He's particularly excited about the new network-based services that require no front investment from him. "This baby is sitting there waiting for us," he says. "They're as close as the nearest telephone line." And one day, Gerstner hopes, network computing will be just as ubiquitous.

*By Ira Sager in Armonk, N. Y., with bureau reports*

*See interview with Lou Gerstner on page 10*

# PRODIGY: A 5-YEAR-OLD UNDERACHIEVER

**W**hen it went online in 1990, Prodigy was a true trailblazer. Corporate parents IBM and partner Sears, Roebuck & Co. had recognized the potential for bringing the information revolution to consumers. For just \$9.95 a month, Prodigy Services Co. offered push-button access to all sorts of information, an electronic shopping mall, and E-mail. In two years, 1 million people had signed up.

By now, Prodigy might well have put IBM out front in the wired world of online services. Instead, with just 1.35 million members currently, Prodigy has become a distant third—after America Online Inc. (AOL) and CompuServe Inc.—and it is slipping farther behind. While Prodigy is expected to add 150,000 subscribers by the end of this year, AOL will triple, to 4.5 million, according to market researcher SIMBA Information Inc. (chart). And after plunking down more than \$1 billion, IBM and Sears have yet to see a sustained profit. According to published reports, Prodigy lost \$3.8 million in 1994 and \$900,000 after taxes in the first half of 1995.

**DEFECTIONS.** The situation looks grim, and some of Prodigy's key content providers are looking elsewhere. On Sept. 28, for instance, the *Los Angeles Times* announced the end of a year-old exclusive relationship with Prodigy. It's moving to the fast-growing World Wide Web, part of the global Internet. There are likely to be defections from AOL and CompuServe to the Web also. But with its smaller audience, Prodigy may lose more content providers more quickly.

Prodigy's new president, Edward

A. Bennett, former head of Viacom Inc.'s VH-1 cable-television channel, believes that the service still has a fighting chance. The third chief in five years, Bennett is concentrating on remaking Prodigy into a more user-friendly portal to the labyrinthine Internet. Prodigy has already developed more than 100 special-interest areas that index Web resources—on subjects ranging from accounting to veterans' affairs. Although both AOL and Com-

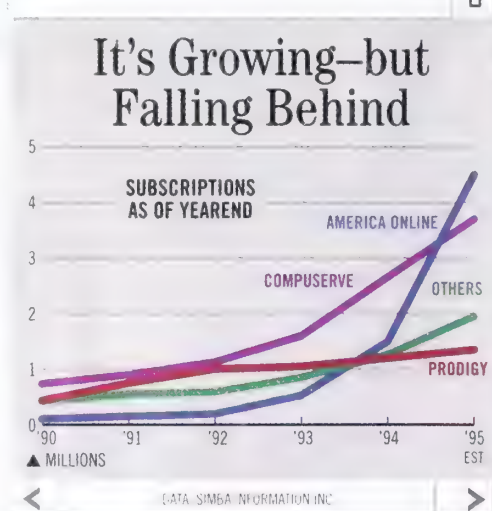
trying to achieve a hipper image with a new \$10 million advertising campaign, including a series of slick prime-time TV spots. And in October, the company hired several executives who may help bring in fresh material. Heading Prodigy's business development, for example, is David Friedensohn, a former entertainment-industry consultant whose clients have included Viacom New Media and NBC.

**READY TO SELL?** Still, that may not be enough to heal the company's ills. Several of the company's top managers have left, including No. 2 Scott Kurnitt, who as executive vice-president had pushed hard for change at slow-moving Prodigy. And despite its quick adoption of the multimedia Web, the service still suffers from a somewhat stodgy image.

Clearly, Prodigy can't continue on its downward course indefinitely, and IBM Chairman Louis V. Gerstner Jr. says he will resolve the situation soon. One possible way would be to buy out Sears' half and gain complete control of Prodigy, then focus on making it work. In August, Sears announced

that it was "assessing [its] strategic position in Prodigy"—sending the signal that, for the right price, the retailer would be prepared to sell. Insiders are excited over this sellout possibility. They're hoping that IBM will then find new partners—an entertainment giant such as Viacom, for instance—that will help to restore Prodigy to its former success. Otherwise, this onetime child star might not survive into adulthood.

*By Paul M. Eng in New York, with Susan Chandler in Chicago*



puServe also offer links to the Web, those services are just now linking Web sites to content that has been created specifically for their networks. The Internet strategy, says Michael Rogers, managing editor of *Newsweek Online*, is one reason the newsweekly is staying put. "Prodigy is really way ahead" in adapting to the Internet, he says.

Meanwhile, Prodigy is on the prowl for fresh content. It has new offices in Los Angeles and New York to woo entertainment giants. It's also



Citation X

## What price speed?

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VII require a stop\* to complete the mission. Astra SPX is the business jet that leaves the others up in the air.

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\*The graph compares business aircraft on a non-stop flight from New York City to Los Angeles. B/C/A assumes a 100% load factor.

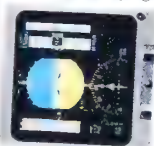
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mid size competitors. In fact, the SPX can take off from shorter fields than the Beechjet 400A and has a lower operating cost per mile than the Citation V Ultra.

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"The Astra SPX will score an A+ in the knots-per-dollar-of-purchase-price category on the chief financial officer's tally card," says B/C/A. The Astra SPX is part of a new generation of Astra business aircraft designed for corporations, large and small, looking at new ways to reduce overhead and improve profits. After all, it all comes down to the bottom line.

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# LOU GERSTNER ON CATCHING THE THIRD WAVE

IBM's CEO sees online computing driving all his businesses

**L**ouis V. Gerstner Jr. caused a stir two summers ago when he declared that the last thing IBM needed was to proclaim a grand vision. Gerstner proceeded to focus on cost-cutting and other management issues and proved the vision-hungry pundits wrong. But having studied IBM, the computer industry, and technology trends, the former McKinsey & Co. consultant has come up with, if not a vision, at least a plan for IBM. Relaxing in a conference room where he keeps a couple of computers to check out everything from kids' software to Web browsers, Gerstner shared his ideas with Information Processing Editor Ira Sager.

**Q:** You speak of "network-centric" computing. What is it?

**A:** The first wave of computing, 30 years ago, was driven by the technologies of host-based processors [mainframes] and storage devices. Twenty years later, we moved into a second wave, which was driven by microprocessors and simplified operating systems. The third wave of computing is being driven by very powerful networked technologies that provide very inexpensive and very wide [communications] bandwidth.

**Q:** What will happen to existing computers?

**A:** People have argued that the host-based [mainframe] model is dead. Well, it isn't dead. People are buying more of those units than they ever have. And no one should say that the stand-alone personal computer is going to go away. But there is no question that the PC-based model is now not the future. The future is a network-centric model. The focus moves to a network that draws out the best of both worlds. That model drives the strategy of this company. When people talk about IBM, it's interesting to hear them say: "Well, I won-

der if they'll get their new businesses to grow fast enough while their old businesses die." What they don't understand is, we are reconceptualizing our old businesses. We're bringing them into this new model.

**Q:** Will IBM put applications on a network and charge per-transaction or volume-based fees?

**A:** Absolutely. We call this business



**“There is no question that the PC-based model is now not the future”**

— LOU GERSTNER, IBM

process outsourcing. For example, this Internet or networked world will put extreme pressure on traditional providers of financial services. We have no interest in going into the banking business. But we do have an interest in working with a series of banks in which we will provide networking capability through the IBM Global Network

and networking applications that we will build. We'll take part of the transaction revenue. It could very well be on a per-click, per-communication unit. It is a strategy that brings our customers into this world of network services. Yes, we will be compensated in nontraditional ways.

**Q:** That provides a recurring source of revenue—as opposed to one-time product sales. Is this where you see network computing leading IBM?

**A:** That's the model IBM created with its mainframe software—monthly license revenue. We understand the concept of software paid for on a usage basis as opposed to a shrink-wrap, buy-it-once basis. Now, all of this is going to take time. It's going to evolve differently in different industries, in different companies, depending on their strategies. Large customers are going to take a very long time before they're going to rent mission-critical applications. People will not convert their own legacy systems to this. What will go on a rental model is the new stuff, like electronic commerce.

**Q:** In a wired world, must IBM remain a big maker of hardware and software?

**A:** People are going to need a lot of very powerful servers. They're going to need a lot of transaction software. They're going to need a lot of database software. They're going to need a lot of communications software. You don't necessarily have to provide all of those things, but we do. And as long as we're successful in each of them, we're going to continue to provide them. If we're not successful, we'll get out of the business.

**Q:** How does Prodigy fit into IBM's network-computing plans?

**A:** We are taking a hard look at our Prodigy strategy right now, along with [Prodigy partner] Sears. Short term, we're making a lot of changes.

brought in new management. They've done some new things with their system. Certainly their merchandising and marketing has gotten better. But their long-term strategy for Prodigy and Prodigy is not clear. We will sort that out in

relatively short time. The fundamental issue is: In the world of the Internet, is there a place for a package of services? Does the customer want to go surf the Net and go to every one of 50,000 Web sites? Or will people pay a reasonable amount for somebody to go out and preselect and package what they want. My guess is they will both coexist.



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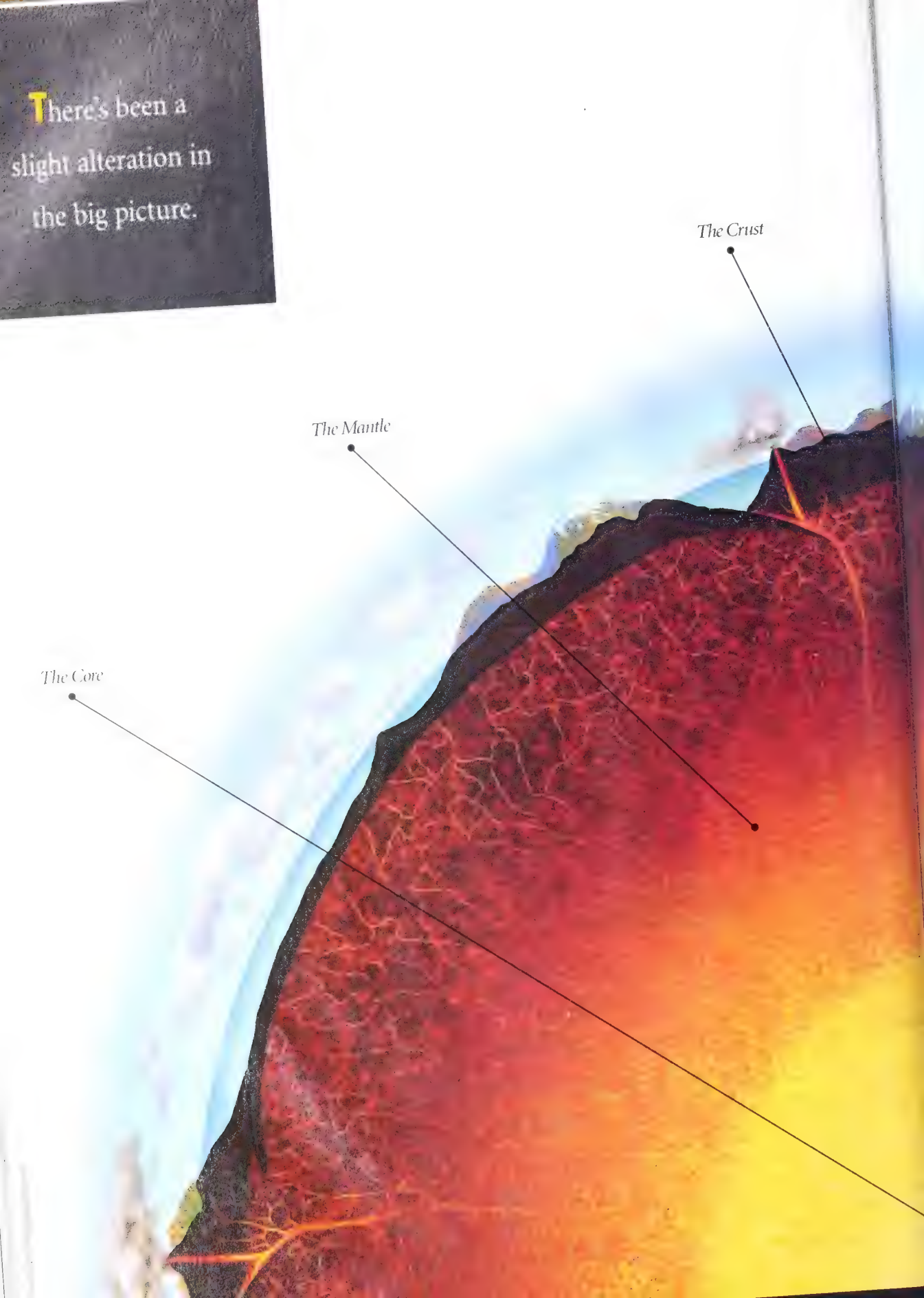


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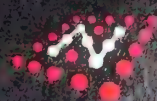
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## THE GOOD OLD DAYS

When rackets were wooden and Everet was sizzling, tennis was never hotter

## TENNIS

# NOW THE BALL IS IN TENNIS' COURT

How the spoiled brat of big-time sports is reaching out to remake its image

**W**hen the tennis boom peaked in 1978, more than 35 million Americans played the game. It was still the era of wooden rackets, and a record 8 million were snatched up in 1976, mostly by the baby boomers who fueled the growth of the sport. Waiting lines were a common sight at public courts, the legendary Chris Evert-Martina Navratilova rivalry was starting to sizzle, and a brash, young upstart named John McEnroe was launching his assault on the domination of Bjorn Borg and Jimmy Connors.

Tennis was hot.

Then suddenly, and for no single reason, it was not. Participation dwindled to 21 million by the late 1980s, and with the dawn of the 1990s, an overall decline—both in playing and watching—continued. Streams of stories—

such as *Sports Illustrated's* 1994 cover "Is Tennis Dying?"—complained about dull, spoiled superstars and shook the industry. By the time Monica Seles was stabbed by a deranged Steffi Graf fan in Hamburg in 1993 and wunderkind Jennifer Capriati was arrested on marijuana charges in 1994, tennis had a serious image problem.

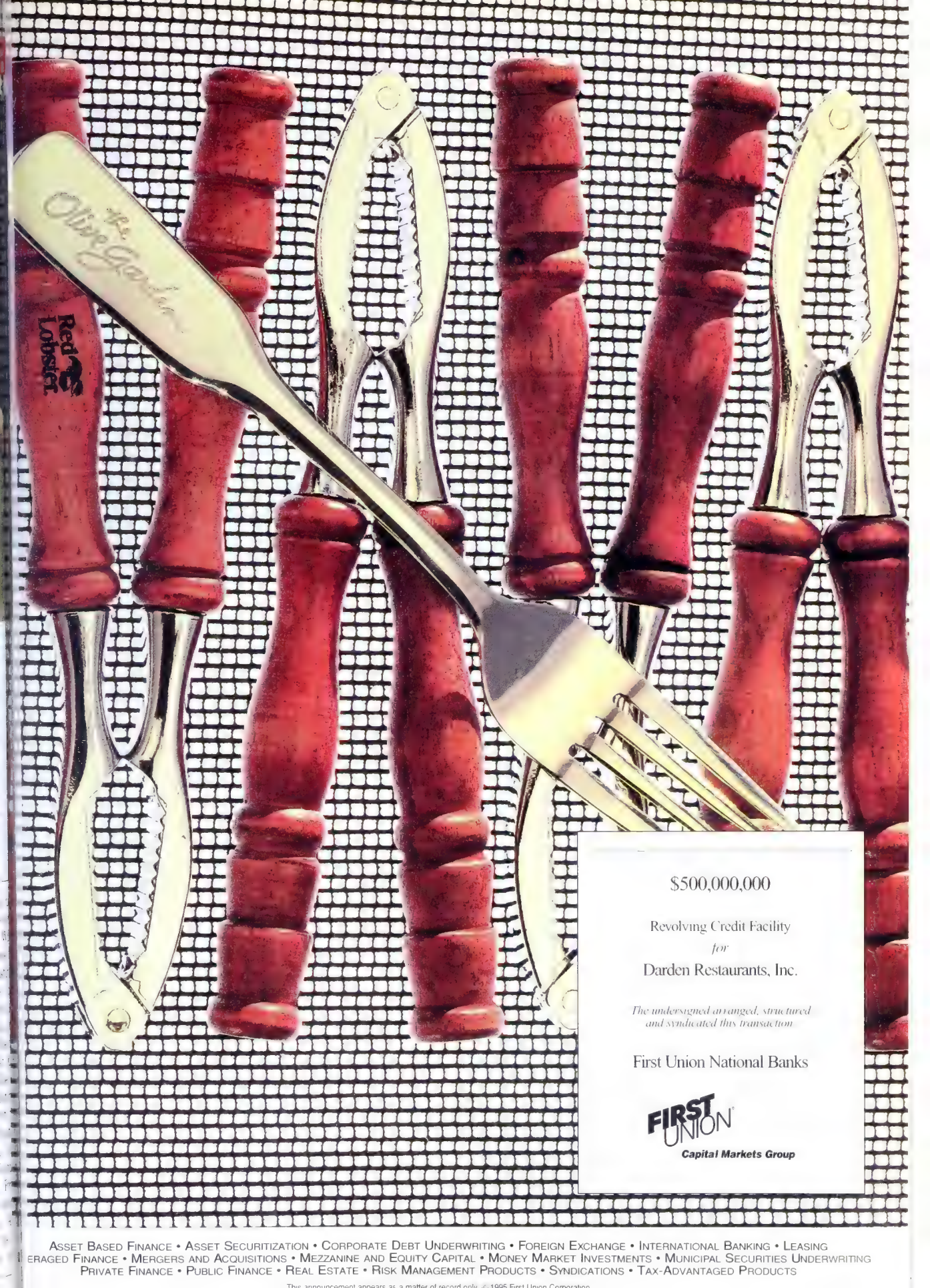
**BLESSING IN DISGUISE.** In the past four years, retail sales for tennis products have dropped by 40%. Fewer than 18 million Americans now take to the courts, according to the Tennis Industry Assn. (TIA), and tennis has plummeted from 8th at its height to the 26th-most-popular participatory sport: A recent survey even placed it behind George Bush's other favorite, horseshoes.

But the bottoming-out of the tennis biz may prove to be a blessing in dis-

guise. "It's been a nightmare in many ways," says James Baugh, vice-president and general manager of Wilson Sporting Goods Co. "But I also see it as a rallying point to pull this industry together and get behind the one brand name that really matters, T.E.N.N.I.S."

Under the umbrella of the TIA, once icy industry rivals have gotten the message that unity may be the best medicine for what ails tennis. So earlier this year, the TIA launched its "Initiative to Grow the Game," with support from more than 130 member organizations including the U.S. Tennis Assn. (USTA), ATP Tour, and WTA Tour; manufacturing powerhouses such as Wilson, Prince, and Head; and individuals such as Evert, Navratilova, McEnroe, Andre Agassi, and Pete Sampras. The campaign's lofty aspirations: to cre-





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500,000 new tennis players in the U.S. while changing the elitist image of tennis, especially among young people.

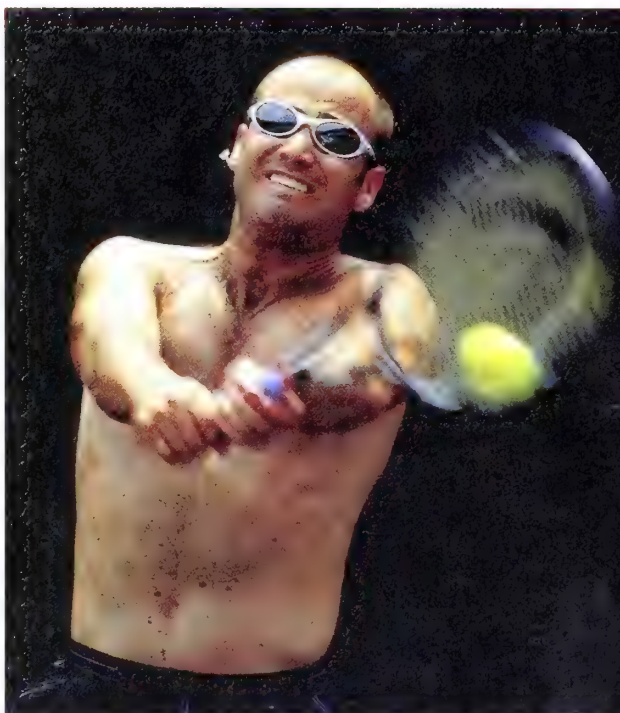
The \$15 million, three-year initiative—with industry manufacturers, associations, and individuals collectively picking up the tab—is the first time tennis has attempted to market the game itself. Says TIA Executive Director Brad Patterson: "Everyone in the tennis business finally agrees that we need to work together...and create a whole new wave of popularity for the sport."

Central to the TIA's initiative is a free 90-minute group lesson that leads participants into Play Tennis America, an inexpensive, natural follow-up program created by the USTA. Conducted nationwide by more than 3,000 teaching pros, the free lessons have been held in over 20 cities since March and have attracted more than 25,000 new players to the courts.

Better yet for the TIA, survey results say that of the free-lesson participants, three-quarters had never played the game or had stopped playing, while 96% said they would recommend the game to a friend. More important, 84% thought it was "cool," which bodes well for perhaps the most crucial element of the push to remake tennis: the recently unveiled, \$7.5 million, three-year Image Campaign, spearheaded by New York ad agency Warwick Baker & Fiore Inc.

"We were really concerned that if the youth audience hasn't been introduced to tennis by the time they're teenagers, then you've probably lost them forever," says John Sloan of Warwick Baker. "If it's a hot sport among teenagers, [it] will spread all over the place."

Sixty-second radio ads feature hip teens touting the thrills of tennis. In



## THE GOOD NEW DAYS?

At long last, "people give a rip about... players" again. Agassi's string of endorsement contracts can attest to that

one spot, a teen enthusiastically talks himself through a tough match. "O.K., the next one. In his ear. Eat that, sucker. This is my court. Listen to the crowd. Ahhh, my serve. Oh, in your shorts! So sorry!" The ad's closing slogan, "Put Yourself on the Line. Play Tennis," will also be featured on promotional posters, postcards, T-shirts, and flyers. In 1996, TIA officials hope to expand the image campaign to as many as 15 major markets, while the free-lesson program is expected to reach approximately 40 cities next year.

**"COOLER SPORT."** Are all these efforts working? Ratings for the U.S. Open's Super Saturday were up more than 40%—the best viewership in four years. And a sport often criticized for having too few personalities suddenly seems flush with them. Says CBS analyst Mary Carillo, a commentator during the dramatic Sampras-Agassi and Graf-Seles

matches at the Open: "Tennis ratings are personality-driven. That's exactly why the ratings were good—because people give a rip about those players."

Corporate America appears to be getting more interested, too. Agassi, already the king of tennis endorsements with deals estimated at \$9.5 million

last year, signed with PepsiCo Inc. during the Open. For \$2 million to \$3 million over two years, he will pitch Mountain Dew in the U.S. and Pepsi Max more than 50 markets outside the U.S.

"There's been a ton of publicity about how Agassi and Sampras have revitalized the game, and that's important," says Pepsi spokesman Brad Shaw. "Tennis certainly has changed, and it's become a hipper, cooler sport. And because of guys like Agassi, we are more inclined to link with it."

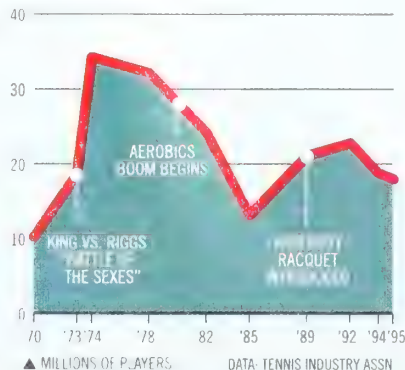
At the same time, the WTA Tour without its title sponsor since Kraft Foods Inc.'s departure in 1993—in effect, October accepted a three-year, \$12 million deal from Corel Corp., the Canadian software company. In a parallel move, the ATP Tour—faced with title sponsor IBM's departure at yearend—has already signed a four-year, global deal with Mercedes-Benz, estimated to be worth \$10 million.

Nike Inc. recently added Seles to its stable of stars that includes Agassi, Sampras, Jim Courier, and Mary Pierce. Its enthusiasm might have something to do with the 102% climb in sales of Nike men's tennis apparel over 1995. "The top players are creating excitement again," says Donna Gibbs, Nike's director of corporate communication.

They are also doing more than just talking up tennis. In February, the president of the ATP Tour launched the \$1.5 million Kids' Fund program, underwritten with contributions from their prize money pool. And the top-50 ranked players

## The Faded Glory of Tennis

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have vowed to commit a total of 500 days to programs such as Kids' Days, in which youngsters are provided with tickets to ATP events, clinics, trading cards, and autograph sessions with top players. The players are also taking part in Smash Tennis, a street-festival-style celebration of the game that includes skill contests, entertainment, and music. "We need to get kids playing again," says Sampras, who spent several hours hitting, answering questions and hanging out with local youths during the Lipton Championships in Key Biscayne, Fla.. "You know, instead of picking up a basketball or football, let's put a tennis racket in their hands."

A progressive shift is also taking place at another long-criticized group, the USTA. In the afterglow of one of the biggest Opens ever—officials say sponsorship interest has never been higher—the USTA recently announced a \$600,000 donation to four inner-city youth programs, while the \$1.25 million the USTA earmarked for Play Tennis America this year was the largest single contribution to the TIA's initiative.

**REAPING THE REWARDS.** An increasingly cohesive tennis industry is already reaping some benefits. Recent indications from retailers show tennis sales are up by as much as 14% in some outlets, the first good news for the manufacturers in years. And companies such as Prince, Dunlop, and Wilson expect the new, longer rackets—1 inch to 2 inches longer than standard 27-inch frames—to become hot items and boost retail sales even more.

But industry leaders, while excited about recent developments, are keeping their feet on the ground. The consensus is that any substantial impact on the public image of tennis—whether through media campaigns, free lessons, or increased involvement from the big-name pros—is not going to happen overnight. Says Rick Margin, vice-president for marketing at Prince and chair of the TIA's Image Committee: "Any attempt to change an image as deeply ingrained in society as [that of] tennis is probably a three- to five-year process." Adds Carillo: "I don't think tennis is out of the woods by any stretch. It's still considered an elitist game."

Sure, in the era of inline skates, beach volleyball, and kids glued to their PCs, a new tennis boom seems like a reach. Yet if the image campaign can draw thousands of new players to the courts and create a more contemporary image, at the least the sport could stop its slide. Who knows, it might even snag a few of those grumbling fans fed up with the hickory heads of baseball.

Tennis, anyone?

By Mitch Rustad in New York

## Economics

### POLICY

# THE GREAT GROWTH DEBATE

CEOs' economic optimism is fueling candidates' rhetoric

**D**on't tell Dana G. Mead that the U.S. economy can't grow faster. The Tenneco Inc. chief executive has seen his company's efficiency surge since it reorganized, cut its payroll by more than a third, and invested heavily in everything from shipyards to office automation. With similar gains spreading throughout Corporate America, "there's no reason why we can't get growth back to what we're used to in this country—3.5% [a year] or more," says Mead. "We've got the industrial wherewithal to do it."

Welcome to the great growth debate. Business leaders, enjoying rapid productivity gains in their own companies, are charging that the economy's growth is being squelched by Washington. Their favorite culprits: Clinton Administration and Federal Reserve economists, who calculate that the U.S. economy can't persistently grow faster than 2.5% a year—only slightly better than its current 2% pace—without boosting inflation. "There's no sign of pricing pressures anywhere," grouses John F. Welch Jr., CEO of General Electric Co. "This economy can grow more than 2% or 2.5%, and we ought to let it do it."

If the economy could just do it, faster growth could work wonders. The federal budget deficit would shrink markedly (chart). Real wages could climb as companies share the rewards of greater efficiency with workers. A rising tide of growth could ease social strains by creating new jobs. Little wonder that economists from both the left and right are scanning the horizon for evidence of stronger potential growth.

But skeptics say the economy's happy days of fast growth haven't returned. Economic statistics are murky when it

comes to the productivity gains that CEOs trumpet. Fed officials, while denying they've set an economic speed limit, argue that signs of overheating during 1994's growth surge keep them off the accelerator for now. And administration economists don't want to lose a hard-won reputation for honest forecasting by bringing back "Rosy Scenario" from the Reagan era.

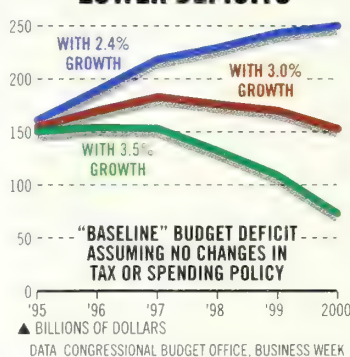
For Republican Presidential candidates, this mixture of CEO discontent and Washington caution is a godsend. As the election nears, GOP has a problem: President Clinton's boast of a solid economy, with unemployment near a six-year low. The Republican response is to shift the focus to the economy's long-term

tential. The front-runner, Senate Majority Leader Bob Dole (R-Kan.), charges that Clinton believes "we can't even live up to our past, much less compete with the most dynamic economies in the world." Long-shot candidate Steve Forbes has made growth a campaign centerpiece. "Americans have great expectations—they don't like the ideal limits," says GOP pollster Fred Steer. "Growth is a good Republican theme."

**A BOOM.** Whether it's good economic growth is a thornier question. Over the long haul, the economy's noninflationary growth rate is a sum of two items: growth in the labor force and growth in productivity, or output per hour of work. With labor growth projected to be about 1% per year through the end of the decade, workers would have to boost their productivity sharply from the trough of the 1980s to lift growth trends.

True, the U.S. is enjoying a productivity boom at the moment. Led by manufacturing, nonfarm productivity

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C A N

**Canon**



been rising by more than 2% a year in the 1990s. But doubters argue that recent gains are largely the normal increase associated with recovery from recessions. They say there is little reason to believe that underlying productivity has sharply improved from its average rate of around 1% in the 1980s—barely enough to support 2.5% economic growth. And a new system for measuring gross domestic product, which the government will adopt by yearend, will revise productivity downward somewhat. To growth skeptics, such as Charles Lieberman, director of research at Chemical Securities Inc., unemployment at a low 5.6% indicates that the economy is already running close to top speed.

Yet many economists believe the statistics are deeply flawed. The optimists, liberal and conservative alike, say the economy's growth potential is sharply higher than in the '70s and '80s. The Fed can't accurately measure overheating, argues Merrill Lynch & Co. Chief Economist Donald H. Straszheim, because production capacity has been growing faster than most economists expected. "Lots of companies

are producing 40% more than they were a few years back with the same equipment and workers, just because of process improvements," Straszheim says.

What's more, advances in service-sector efficiency—such as the replacement of bank tellers with automated-teller machines—are ignored in the government's productivity numbers. Statisticians also miss a lot of price and quality improvements in high-tech products, from semiconductors to telecom gear. Anecdotal evidence abounds that corporate restructuring and smarter use of technology are making workers far more productive (BW—Oct. 9).

In this case, CEOs' gut feelings may tell more about the economy than do official figures—and CEOs are bullish. In a September survey, 73% of the directors of the National Association of Manufacturers said the U.S. economy could grow at a 3% rate or faster for the re-

mainder of the decade, without boosting inflation. "Whether the government counts it or not, we know this productivity is real," says Tenneco's Mead, who chairs NAM. The organization wants the Fed to cut interest rates to boost growth now, and calls on Washington to lift potential growth even higher by balancing the budget, overhauling regulations, and expanding trade.

**REALLY ROSY?** Throw in some tax cuts, and that's an agenda many in the GOP would love to run on. Republicans figure that the growth debate can only help them—provided the public overlooks

Williamsburg, Va., on Oct. 13 made it clear that they want to see a stronger economy. When the President spoke, the business leaders and their spouses stood stone-faced through his spirited defense of his record on cutting regulations and reinventing government. He drew applause for only two lines—on gun control and nuclear nonproliferation.

While the White House dodges big bats, the power center that controls the economy's throttle—the Fed—is divided. Some policymakers, such as San Francisco Federal Reserve Bank President Robert T. Parry, believe the econ-

## FASTER, FASTER



**DANA MEAD** CEO, Tenneco



**DONALD STRASZHEIM** Economist, Merrill Lynch



## TAKE IT EASY



**LAURA TYSON** National Economic Council



**CHARLES LIEBERMAN** Economist, Chemical Securities

some details. In the budget battle on Capitol Hill, for example, the Republican leadership insists on using a forecast of 2.3% annual growth for the next seven years—even lower than Clinton's 2.5%. "While Dole says we're pessimists, his budget committee accuses us of being too rosy," says National Economic Adviser Laura D'Andrea Tyson. The GOP figures the low forecast gives them a bargaining chip during negotiations with the White House.

Clinton, however, seems stuck. His version of the progrowth agenda—slower budget cuts that protect spending on education, training, and government-led R&D—doesn't resonate with business. And in defending its 2.5% forecast, the Administration worsens its relations with Corporate America. CEOs at a Business Council meeting in Wil-

liamsburg, Va., on Oct. 13 made it clear that they want to see a stronger economy. When the President spoke, the business leaders and their spouses stood stone-faced through his spirited defense of his record on cutting regulations and reinventing government. He drew applause for only two lines—on gun control and nuclear nonproliferation.

Under Greenspan's strategy, growth debate will eventually be settled: As inflation stays low, the high potential that CEOs trumpet will be growth upward. But the prospect of a stronger economy in the future is unlikely to satisfy either business or voters. As candidates wrap themselves in the growth mantle, business will be turning up the heat on Washington to make faster growth a reality.

By Mike McNamee in Washington with Christopher Farrell in New York

WHEN SELECTING A  
Mutual Fund FOR A 401(k) PLAN,  
NAMES CAN BE *Deceiving.*



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# Introducing new **Microsoft Office** for Windows 95

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Software that doesn't get in your way when you're trying to work.**



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work the way you always hoped they would.**

New Microsoft® Excel, Word, PowerPoint®, Microsoft Access, and Schedule+. Use them to work more effectively, to access and share information throughout your company, to conduct more in-depth analysis. Pull information from one application



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Combine a cover letter, financial projections, and professional-looking charts and graphs seamlessly into one document. Save and print it as one. Open it and have all the applications it uses launch at once. You spend less time going back and forth between programs. Less time working around obstacles. More time focusing on the task at hand.

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You find new ways to communicate, to share information, to collaborate.**

Now you can use Microsoft Word as your e-mail editor with the Microsoft Exchange Inbox in Windows 95. Create your messages in Word, and use all of its functionality, its formatting options, to communicate more clearly, more convincingly. With Word's Internet Assistant,\* you can browse the World Wide Web and publish your own documents there. If you subscribe to The Microsoft Network, you can access it directly from Office. FindFast lets you search company servers and individual desktops for information you need by typing a phrase or keyword. Even finding the information you need to schedule a meeting is made simpler with the Meeting Wizard in Schedule+. It can find a time when your list of people can meet, locate a conference room, and notify everyone of the time and place.



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EDITED BY AMY DUNKIN

## THIS TAURUS SURE WON'T BLEND INTO THE CROWD



The redesigned '96 Ford Taurus, with its futuristic elliptical look, is actually an anachronism. Automotive experts predict that the 21st century will be the age of the niche car and that mass models, such as the Taurus, will face the fate of their extinct ancestors, the Chevy Impala and Ford Galaxy, which a generation ago each sold more than 1 million units a year.

So how can the No. 1 Taurus hold on to its sales crown in an evaporating market? It has to steal sales from the competition, particularly the Japanese. And with the new Taurus, Ford's designers have stretched beyond Detroit's comfort zone to come up with a sedan that is visually striking and remarkably nimble on the road. The payoff for Ford's \$2.8 billion overhaul of the Taurus and its Mercury Sable twin is a car that finally gives Detroit, or at least Ford, some

hope of prying baby boomers out of their Honda Accords and Toyota Camrys.

On first glance, it's styling that sets Taurus apart from its Japanese and U.S. brethren. The jelly-bean shape of the original

Taurus was groundbreaking and controversial back in 1986. The 1996 Taurus doesn't entirely eschew the aerodynamic look, but it is spiced with much more attitude than its now-dowdy parent. Beneath the furrowed brow of its cat's-eye headlights and

undulating hood, the new Taurus appears to be scowling. The audacious styling is sure to set off the same kind of love-it-or-hate-it debate inspired by its predecessor. This is one family car that will not blend into the crowd at the grocery-store parking lot.

What strikes you next is Taurus' seemingly compact size, with its sloping nose and droopy haunches. Most people say initially: "It looks smaller." But it's not. It actu-

### TAURUS LX

Base Price:

**\$21,530**

*Audacious styling and a nice taut ride*

ally is a foot longer than the Camry and nearly half a foot longer than the old Taurus. This illusion is an ingenious move by Ford designers to satisfy women drivers who

were turned off by the bulkiness of the old Taurus but who still wanted plenty of interior space. By burnishing the edges and repeating soft, oval theme throughout the design, the Taurus just looks easier to handle.

There are trade-offs with





melted-butter-stick styl-  
By rounding the rear  
Ford made the Taurus'  
k 2.5 cubic ft. smaller  
its predecessor, taking  
more than 10% of its  
e. That is a noticeable  
especially for the fami-  
and businesspeople who  
his trunk all the time.  
navigating the curvy  
door openings can be  
v, especially when plac-  
hildren into car seats.  
e yet, the sculpted  
forced Ford to reduce  
room in the back.  
ll, this minimalist-design  
e actually has Japan  
ing Detroit for a change.  
amry, which has bloated  
lerably over the years,  
ently will lose some of  
lk next year: Those who  
seen the design for Toy-  
revamped 1997 Camry  
is much slimmer than  
urrent model.

**EDGE.** Toyota and  
also are trying to put  
prices on a diet. Each  
ese auto maker is strip-  
ts flagship sedans of un-  
sary parts and features  
e thousands of dollars  
the yen-inflated prices.  
1996 Camry XLE V6 se-  
nas a base price of \$16,  
8, including destination  
s. The 1996 Honda Ac-  
x V6 sedan starts at  
20.

With the new Camry  
r off and the Accord  
years from its next  
ver, the Taurus will en-  
considerable price ad-  
re for the near-future.  
Taurus GL, equipped  
n enhanced version of  
-liter V6 engine found

in the previous model, comes  
with air conditioning and  
power windows for \$19,390.  
The Taurus LX, with an im-  
pressive new high-perform-  
ance multivalve V6, starts  
at \$21,530. The 200-horse-  
power Duratec engine prop-  
els the LX from zero to 60  
mph in 8.4 seconds.

building the new Taurus on  
an extremely rigid frame,  
Ford has achieved a taut feel  
for the road that is much  
closer to the Japanese sen-  
sation than it is to Detroit's  
sad history of squishy, boule-  
vard rides. The Lumina,  
which improved measurably  
with its redesign last year,

the center of the dash, puts  
stereo and climate controls  
within easy reach. Gone are  
the Chiclet-size radio buttons  
that were dangerous diver-  
sions from the road. They  
are replaced by a rising row  
of spacious, stepping-stone  
buttons that can be quickly  
found without looking. The  
control panel is an-  
chored by a big,  
easy-to-grab volume  
knob located beside  
a stylish, teardrop  
LED screen that  
displays the time  
and radio station  
separately.

Another interior  
marvel is hidden in  
the front seat of the  
six-passenger ver-  
sion. The center of  
the front seat un-  
folds like a Swiss  
Army knife to reveal  
a console that can  
hold three cups and  
even a cellular  
phone, if you have  
Ford install one. But  
if you have one of

the more popular portable  
cellular phones, you can't  
plug it into the lighter port  
when the console is unfurled  
because the ashtray on the  
dash gets blocked. Ford offi-  
cials say they have received  
several complaints about this,  
so they are adding another  
power outlet, to the console,  
by the end of the year.

That kind of quick response  
should impress demanding  
baby boomers who in the past  
have snubbed the Taurus. If  
they take a look at the new  
version, they will find interior  
creature comforts that clearly  
top what they are accustomed  
to in their Accords and Cam-  
rys. And they will experience  
ride and handling that is com-  
parable to their beloved Japa-  
nese sedans.

The mass-market car may  
indeed be an endangered  
species. But if Ford's bold  
new sedan wins over that  
lost generation of family-  
car buyers, the Taurus may  
yet manage to avoid the  
fate of the Impala and the  
Galaxy. *Keith Naughton*

## Following the Leader



### CHEVROLET LUMINA SEDAN

Base Price:

**\$16,895**

*Low cost, but  
no match for  
Taurus' ride*

### TOYOTA CAMRY XLE V6 SEDAN

Base Price:

**\$22,868**

*Its price and  
bulk are due  
for a trim*



Taurus' U.S. competitors  
give it more of a run for its  
money on sticker price. The  
price-leading Chevrolet Lu-  
mina starts at \$16,895, while  
the Dodge Intrepid has a  
base price of \$18,995. One  
disappointment in the domes-  
tic family sedans: Buyers  
have to pony up about \$600  
extra for antilock brakes,  
while the V6 versions of the  
Camry and Accord make  
those safety brakes standard  
equipment.

When the cars hit the  
road, Taurus parts company  
with its Detroit rivals. By

still feels choppy over bumps  
and wallows into turns. The  
Taurus holds the road around  
tight corners, and its four-  
wheel independent suspen-  
sion absorbs potholes with  
precision. The Intrepid re-  
ceived some much-needed  
noise reduction for the 1996  
model year. But it's still no  
match for the Taurus, in  
which a driver and rear-seat  
passengers can talk without  
raising their voices.

**CREATURE COMFORTS.** Com-  
pared with the Japanese  
cars, the Taurus holds its  
own on the road. The Camry  
still has a smoother shifting  
transmission and the Accord  
has a tighter ride. But on  
balance, the Taurus makes so  
much improvement in steer-  
ing, handling, and braking  
that it now can be consid-  
ered in the same league as  
those superior sedans.

The interior of the Taurus  
continues the oval design  
motif, with a supremely  
user-friendly control panel as  
its centerpiece. The tactile  
control pod, mounted high in

### CAT'S MEOW?

*Ford Taurus'  
futuristic  
elliptical  
motif and  
cat's-eye head-  
lights punctu-  
ate a redesign  
that is aimed  
at keeping the  
car No. 1 in  
an evaporat-  
ing market*







## SATURN SL2 SEDAN

Base Price:

**\$12,685**

*Still a solid choice after undergoing cosmetic surgery that added some pizzazz and headroom*

But General Motors has made worthwhile improvements for 1996. A rounder and curving rear end give the car a little more pizzazz and more headroom. Extra insulation and a new valve make the car considerably quieter at high speeds, though the 1.6-liter engine runs smoothly, although it still sounds a bit

## TWO TOP-NOTCH COMPACTS BECOME EVEN MORE SO

**Radio personality Garrison Keillor used to joke that Lake Wobegon was a place**

where the children were all above average. One could also easily say that about the compact-car market: When motorists can choose among the

Honda Civic, Saturn, Toyota Corolla, Ford Contour, and Plymouth Neon, there's no need to settle for mediocrity.

With that in mind, I spent a couple of weeks test-driving the Civic and Saturn, two sales leaders that have been redesigned for 1996. The Civic has been completely overhauled, while the Saturn merely got a face-lift.

The new Civic still comes in three styles: hatchback, coupe, and sedan. Although the exterior has been completely redone, the styling of the coupe and sedan is sedate. Aside from larger headlamps and taillights, they look very similar to the Accord. The hatchback has a stylish European look, thanks to the steeply raked rear hatch. The Civic's real attraction is inside.

All three models come with a 1.6-liter engine that loves to be revved. The CX, DX, and LX sport a 106-horsepower engine; the EX gets a 127-hp VTEC power plant.

Thanks to sound-absorbing insulation and a stiffer engine block, the new Civic is much quieter. All dashboard controls are positioned high on the instrument panel, allowing the driver to fiddle with the radio or heater without glancing away from the road. The high roofline offers ample headroom, even in the rear. The trunk size hasn't changed, but Honda has added a convenient split rear seat.

Civic drivers will notice a plusher ride. But Honda's major mechanical innovation is one that relatively few American buyers are expected to choose. In early 1996, the Civic

ic HX coupe will carry a continuously variable transmission, which eliminates jolting gear shifts on hills or when passing. The new transmission is quicker from zero to 60 than a conventional automatic, and it's more fuel-efficient: 35 miles per gallon in the city, 41 on the highway.

Despite the improvements, Honda has held the line on prices. Recently, the company announced a 1.3% increase in base prices for all Civic models except the EX. A top-of-the-line EX equipped with standard features—antilock brakes, automatic transmission, air conditioning, cruise control, and power windows—will sell for about \$16,620, including destination charges. That's about the same as a 1995 model and keeps the EX competitive with Saturn. A similarly equipped SL2 sedan should cost about \$15,300, though other options can push the price as high as \$18,000.

For the money, I've always thought Saturn was a pretty good car whose main attribute is a dealer network with a stellar reputation for service.

what harsh at high rpm.

For 1996, GM designed "fuzzy logic" software for Saturn's automatic transmission. The car's computer analyzes the driver's driving pattern and then adjusts the shifting pattern accordingly. The engine revs at higher speeds for aggressive drivers, at lower rpms for sedate ones. Other new features include daytime running lights plus a deck lid that won't spill water runoff into the trunk.

Minor irritants include the front console that bulges out of the dash and a power window switch that controls the side mirror—but not the door. Still, Saturn has earned high grades for quality on the annual J.D. Power & Associates survey, and there's no reason to expect a change.

Which car is better? Personally, I enjoyed the Civic EX with a stick shift, although it wasn't a runaway deal. Others may prefer the Saturn, a solid car with no-nonsense dealer support. With either choice, you're driving a car that's above average.

*David Seidenberg*

## HONDA CIVIC EX SEDAN

Base Price:

**\$16,620**

*A complete overhaul makes for a quieter, friendlier, plusher ride*





# WEAT LESSEE: DIG OUT LOSE HIDDEN NUMBERS

most 30% of all new  
s are leased in-  
ad of purchased,  
from about 19% in

Is it because consum-  
get a great deal when  
lease? Or because deal-  
stand to profit hand-  
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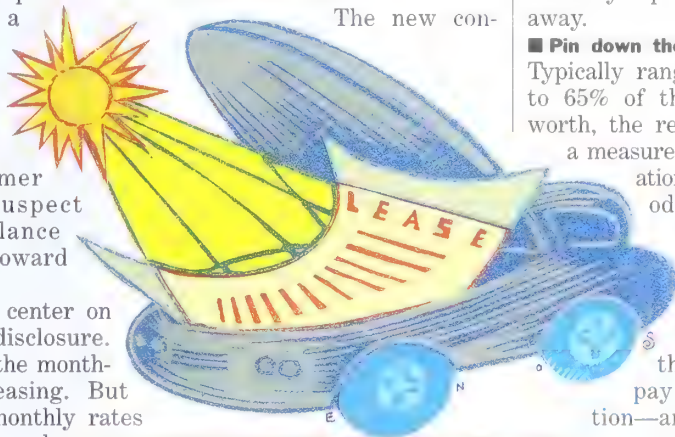
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ve Board, most major  
makers are revising  
lease contracts to pro-  
dditional information on  
early-termination penal-  
and other key points.  
ed, which issued pro-  
amendments to the  
mer Leasing Act in  
eptember, is accepting  
nts from the public un-  
v. 17. Write to William

W. Wiles, Federal Reserve  
Board, Washington, D.C.  
20551, and refer to Docket  
No. R-0892. One specific issue  
the Fed is wrestling with is  
how to create an interest-  
rate number for leasing  
agreements equivalent to the  
annual percentage rate on  
consumer loans.

The new con-



## Leasing Resources

- The Reality Check-  
list, prepared by the  
Consumer Task Force  
for Automotive Is-  
sues, gives tips on  
negotiating a favor-  
able lease contract.  
It's available from  
many state consumer  
affairs offices at no  
cost, or by sending  
\$1.50 and a  
stamped, self-ad-  
dressed envelope to  
Reality Checklist, P.O.  
Box 7648, Atlanta,  
Ga. 30357-0648.

- Expert Lease soft-  
ware helps you calcu-  
late monthly lease  
payments and do a  
lease/buy analysis.  
You can obtain a ba-  
sic DOS version for  
\$59.95 or a just-is-  
sued Windows pro-  
gram for \$129.95  
from Chart Software at  
800 418-8450. Chart  
also offers LeaseTips,  
a five-page, informa-  
tion-packed leaflet,  
for \$5.

DATA BUSINESS WEEK

tracts should help. But if you  
want to lease a car, you still  
have to do several things to  
protect yourself:

- **Negotiate the price.** Then be  
sure the figure you agree  
upon appears on the contract.  
The Fed thinks you should  
know the gross capitalized  
cost of the car—leasing lin-  
go for the rough equivalent  
of the purchase price. Florida,

New York, and New Jersey  
require this disclosure. Some  
new contracts go a step fur-  
ther by including the net cap-  
italized cost, or the price af-  
ter any downpayment or  
trade-in.

Unless this information is  
spelled out in writing, you  
won't know if the  
lessor inflates the  
cost of the car or conven-  
iently "forgets" to reduce the  
price by your trade-in. If a  
salesperson suggests that all  
you need to know is the  
monthly payment, walk  
away.

- **Pin down the residual value.**  
Typically ranging from 35%  
to 65% of the car's initial  
worth, the residual value is

a measure of the depreci-  
ation over the peri-  
od of the lease.

The more the  
car will be  
worth at the  
end of the  
lease period,  
the less you'll  
pay for depreci-  
ation—and the lower  
your monthly pay-  
ments will be.

- **Ask what interest  
rate you'll pay.** This  
is a number you  
won't see on a leas-  
ing contract, even  
the "new and im-  
proved" versions.  
Many industry rep-  
resentatives insist  
that a lease-to-pur-  
chase comparison is  
apples to oranges,  
and that interest  
rates apply only to  
financing, not to  
leasing. But leasing  
costs money, and it's  
nice to know how  
much before you

sign on the dotted line so  
that you can compare lease  
to lease or leasing to buying.

Charles Hart, developer of  
the Expert Lease software  
program, suggests asking for  
the "money factor," a decimal  
number used by most deal-  
ers that may be converted to  
an approximate interest rate  
when multiplied by 24. For  
example, a money factor of

0.00354 converts to a rate of  
about 8.5%, roughly analo-  
gous to today's finance charg-  
es. The factor will vary with  
the length of the lease.

This won't work with  
Ford Motor Credit leases,  
though, because Ford uses  
its own methodology. The  
only way to  
guesstimate the  
interest rate here is to work  
backward from the lease  
charges. Randall McCathren,  
executive vice-president of  
Bank Lease Consultants in  
Nashville, suggests adding  
the net capitalization cost  
and residual value, then di-  
viding by two to get the av-  
erage annual balance. Then  
take the total lease charges  
for the contract term, and  
divide this number by the  
number of years in the lease.  
This annual lease charge, di-  
vided by the average annual  
balance, gives you an ap-  
proximate interest rate.

- **Ask about extra charges.**  
Most leases permit 12,000 to  
15,000 miles of driving per  
year, with a charge of 10¢ to  
as much as 25¢ for every ex-  
tra mile. It's a good idea to  
tailor the lease to your actual  
driving habits. Racking up an  
extra 2,000 miles a year, at  
15¢ per mile, comes to \$900  
at the end of a three-year  
lease.

So-called excess wear and  
tear can also add big bucks  
to the end cost of leasing.  
One lessor's ding in the hood  
is another's significant dam-  
age. Try to pin down the def-  
inition in advance. Early-ter-  
mination penalties can also  
be sizable. Look for a con-  
tract that lets you know up  
front what it will cost to walk  
away early. The Fed's pro-  
posed rules would require a  
dollars-and-cents example of  
the penalty associated with  
ending the lease after the  
first year.

Remember: A good con-  
tract is really only half of the  
battle. If consumers let down  
their guard and rely too  
much on the lease forms for  
protection, they can still find  
themselves caught in bad  
deals. *Grace W. Weinstein*





OFFICIAL  
PGA TOUR  
TENNIS



# THE TOUR Championship



## THE TOUR Championship

The idea was to create a meaningful conclusion to the PGA TOUR

season, a fitting climax to what had evolved throughout the year.

To that end, THE TOUR Championship has more than filled its role.

Introduced in 1987 as the Nabisco Championships of Golf, this elite event for the top-30 money winners has played a significant role in finalizing such prestigious awards as the Arnold Palmer Award for leading money winner and PGA TOUR Player of the Year. Moreover, it has had the final say in team charity payoffs.

No longer does the season simply end. Top players have continued to compete throughout the fall in order to qualify for THE TOUR Championship. It's a matter of money and prestige. Beyond its growth

to a \$3 million purse and \$540,000 winner's share, the tournament continues to provide a final opportunity to go head-to-head against the season's leading players.

"A position in THE TOUR Championship has become one of the most sought after spots in all of golf," said PGA TOUR Commissioner Tim Finchem. "This event was created to not only stimulate year-long interest among our players, but also to provide the TOUR with a fitting climax to its season. THE TOUR Championship has accomplished both missions, and we are very proud of the stature this event has attained in eight short years."

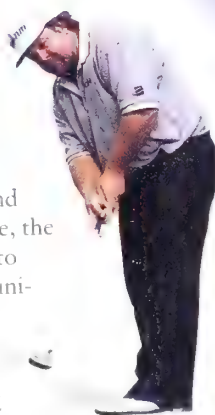
This certainly has proven to be a recipe for viewing excitement. When it comes to generating drama, THE TOUR Championship has excelled. Five times the champion has been determined

in a playoff...including four straight years, starting with Curtis Strange's victory over Tom Kite at Pebble Beach Golf Links in 1988.

That second Championship, in fact, epitomized the intent of the tournament. With the victory, Strange not only clinched both the Player of the Year and the Arnold Palmer Award, the \$360,000 payoff also made him the TOUR's first \$1 million winner in a single season.

Not that the inaugural event at Oak Hills Country Club in San Antonio, TX, was short-changed on significance. Introduced as golf's richest event with a \$2 million purse, it cashed in big with Tom Watson capturing the 32nd PGA TOUR title of his illustrious career and his first in nearly four years.

In fact, the Player of the Year Award also was determined that same week, though not as dramatically as it would be the following year. Strange again was involved, entering Oak Hills as the TOUR's leading money winner. He



needed a solid final week to edge out three-time winner Paul Azinger for the honor. But Strange finished in last place, still earning enough to win the season money title but losing

Player of the Year honors to Azinger, who finished fourth at Oak Hills.

Again, however, it was Strange's victory over Kite the following year – finalized in a Monday playoff after play was suspended Sunday due to darkness – that truly justified the concept of the tournament.

Still vivid in the minds of those who were at Pebble Beach is Strange's brilliant tee shot on the par-3 17th hole, settling 1 1/2 feet from the hole to set up the winning birdie.

Memorable, too, was the impromptu dash to the green by then-Houston Golf Association Executive Director Duke

ler, who gave Strange a thankful, congratulatory hug. The reason for Strange's unabashed exuberance was that Strange's victory also earned \$500,000 for charitable distribution by the Houston tournament, which had drafted Curtis as the PGA TOUR's Charity Team competition.

As if further justification for a meaningful season wrap-up was needed, Kite elected a measure of revenge the following

year at Harbour Town Golf Links on Hilton Head Island, SC, beating Payne Stewart on the second extra hole to earn \$450,000 and clinch his second Arnold Palmer Award with what then was a record \$1,395,278.

Following Kite's lead as a double-winner of THE PLAYERS Championship and Nabisco Championships in the same year was Jodie Mudd, who in 1990 concluded the season by defeating Billy Mayfair on the first playoff hole at Champions Golf Club in Houston.

By 1991, the tournament had taken on a new name – THE TOUR Championship – and a new site strategy by contracting a two-year agreement with historic Pinehurst Resort & Country Club in North Carolina. The tournament was making the rounds of some of the finest golf courses in the country; now, the intent was to remain at the same course for two years.

Remaining constant through these changes, though, was the playoff mode. Pinehurst was christened by Craig Stadler's victory over Russ Cochran with a birdie on the second hole.

THE TOUR Championship finally took a leave from the sudden death format over the next two years, but produced no less excitement.

In 1992, Azinger arrived at Pinehurst with one final gasp to maintain a streak of winning at least one tournament for a sixth straight season. Armed with a strange eye-shaped putter he called

"The Thing," Azinger virtually sealed a three-stroke victory over Lee Janzen and Corey Pavin by holing a 25-foot eagle putt on the 70th hole. His streak remained intact.

THE TOUR Championship next returned to the West Coast in 1993, settling at The Olympic Club in San Francisco for the next two years. And true to the tournament's growing reputation, both years produced memorable finishes.

First it was Jim Gallagher, Jr., winning a wild final-day shootout by one stroke over Greg Norman, David Frost, Scott Simpson and John Huston. Serving as a foundation to his victory was a course record 8-under-par 63 in the opening round.



And last year produced perhaps the most memorable finish of all. After a two-year sabbatical, THE TOUR Championship once again came down to a playoff, this time involving the whistling duo of Mark McCumber and Fuzzy Zoeller.

It lasted only one extra hole, barely enough time for either to pucker his lips. But what a finish it was. Returning to the 18th hole, where McCumber had just bogeyed away his chance for the outright title, the Jacksonville, FL, native got it right the second time around, draining a 50-foot birdie putt for his third victory of the season. It was a memorable finish to the most successful of McCumber's 17 seasons on the PGA TOUR.

#### THE TOUR Championship Television Schedule

Thursday, October 26  
First Round of Competition  
ESPN – 3:30-6:30 p.m.  
Eastern Time

Friday, October 27  
Second Round of Competition  
ESPN – 3:30-6:30 p.m.  
Eastern Time

Saturday, October 28  
Third Round of Competition  
ESPN – 1:30-3:30 p.m.  
Eastern Time

Sunday, October 29  
Fourth Round of Competition  
ABC – 3:00-6:00 p.m.  
Eastern Time

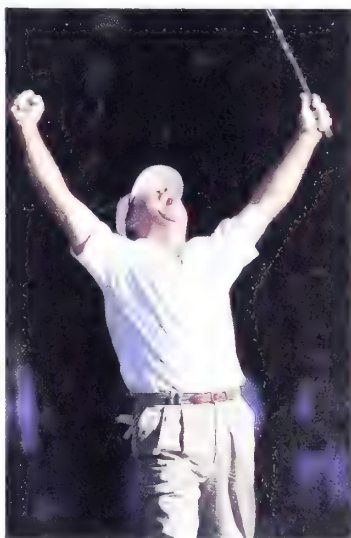
(Note: Standard Time begins at 2:00 a.m. Sunday)

THE TOUR Championship now has relocated to Southern Hills Country Club in Tulsa, OK, for the next two seasons. The site of two U.S. Opens and three PGA Championships, Southern Hills certainly is a worthy host to continue the tournament's growing reputation for excitement and prestige.

Presented by:



Mercedes-Benz



Mark McCumber celebrates after winning THE TOUR Championship.



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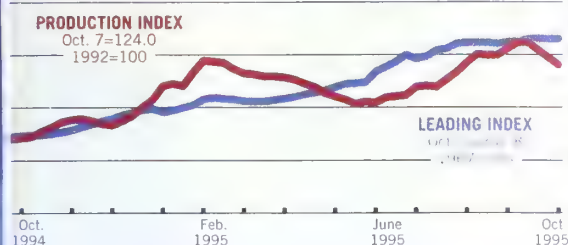
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# Business Week Index

## PRODUCTION AND LEADING INDEXES

Change from last week: -0.6%  
Change from last year: 5.4%

Change from last week: 7.4%  
Change from last year: 7.4%



Production index declined during the week ended Oct. 7. Before adjustment of the four-week moving average, the index also dropped, to 123.6 from 124.5. Cuts in the seasonally adjusted output levels of autos and trucks are the decline.

Leading index was unchanged in the latest week. The unaveraged index rose slightly, slipping to 262.1, from 262.3. A decline in the growth rate of materials prices is a major reason for the weakness.

Production index copyright 1995 by The McGraw-Hill Companies. BW leading index copyright 1995 by IBIS.

## FINANCIAL INDICATORS

|                                            | LATEST WEEK | WEEK AGO   | YEARLY % CHG |
|--------------------------------------------|-------------|------------|--------------|
| <b>STOCK PRICES</b> (10/13) S&P 500        | 580.59      | 582.13     | 24.7         |
| <b>CORPORATE BOND YIELD, Aaa</b> (10/13)   | 7.14%       | 7.20%      | -16.0        |
| <b>INDUSTRIAL MATERIALS PRICES</b> (10/13) | 111.1       | 111.6      | NA*          |
| <b>BANKRUPTCY FAILURES</b> (10/6)          | NA          | NA         | NA           |
| <b>REAL ESTATE LOANS</b> (10/4) billions   | \$497.9     | \$497.3r   | 11.2         |
| <b>MONEY SUPPLY, M2</b> (10/2) billions    | \$3,721.8   | \$3,723.8r | 4.1          |
| <b>UNEMPLOYMENT</b> (9/30) thous.          | 342         | 335        | 7.2          |

Sources: Center for International Business Cycle Research (CIBCR), Standard & Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on bankruptcies and real estate loans. \*Historical data available from CIBCR.

## INTEREST RATES

|                                         | LATEST WEEK | WEEK AGO | YEAR AGO |
|-----------------------------------------|-------------|----------|----------|
| <b>MUTUAL FUNDS</b> (10/17)             | 5.66%       | 5.74%    | 4.72%    |
| <b>COMMERCIAL PAPER</b> (10/17) 3-month | 5.81        | 5.83     | 5.46     |
| <b>SAVING DEPOSITS</b> (10/18) 3-month  | 5.77        | 5.79     | 5.47     |
| <b>MORTGAGE</b> (10/13) 30-year         | 7.72        | 7.78     | 9.08     |
| <b>STABLE MORTGAGE</b> (10/13) one-year | 5.79        | 5.82     | 5.98     |
| <b>TREASURY BILLS</b> (10/18)           | 8.75        | 8.75     | 7.75     |

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

## THE WEEK AHEAD

### FISCAL BUDGET

**Friday, Oct. 23** ▶ The Treasury Dept. is to report a surplus of \$8 billion in October, double the surplus of September 1994. That's the median forecast of analysts surveyed by MMS International, The McGraw-Hill Companies. September is the last month of the fiscal year as a month when quarterly taxes are expected. September surplus means that the fiscal 1995 deficit will be \$163 billion, down from \$203 billion in 1994.

### HOUSING HOME SALES

**Monday, Oct. 25, 8:45 a.m.** ▶ Existing home sales probably sold at an annual rate of

about 3.9 million in September, down from 4.1 million in August. Resales had risen for four straight months before September, but the drop in mortgage applications to buy a home indicates that sales finally posted a decline last month. The recent rally in the bond market, though, suggests one last flurry in home buying before yearend.

### DURABLE GOODS ORDERS

**Thursday, Oct. 26, 8:30 a.m.** ▶ The MMS survey projects that new orders taken by durable-goods producers edged up a small 0.3% in September. Durable-goods producers reported a solid rise in output last month, suggesting stronger demand. New orders jumped 4.8% in August.

## PRODUCTION INDICATORS

|                                                         | LATEST WEEK | WEEK AGO  | YEARLY % CHG |
|---------------------------------------------------------|-------------|-----------|--------------|
| <b>STEEL</b> (10/14) thous. of net tons                 | 1,852       | 1,951#    | -3.1         |
| <b>AUTOS</b> (10/14) units                              | 129,938     | 130,721r# | -7.2         |
| <b>TRUCKS</b> (10/14) units                             | 121,914     | 121,619r# | 1.4          |
| <b>ELECTRIC POWER</b> (10/14) millions of kilowatt-hrs. | 57,917      | 59,654#   | 5.6          |
| <b>CRUDE-OIL REFINING</b> (10/14) thous. of bbl./day    | 13,602      | 14,217#   | 0.8          |
| <b>COAL</b> (10/7) thous. of net tons                   | 19,976#     | 20,641    | 7.8          |
| <b>PAPERBOARD</b> (10/7) thous. of tons                 | 848.0#      | 855.0r    | -4.2         |
| <b>PAPER</b> (10/7) thous. of tons                      | 828.0#      | 819.0r    | 1.8          |
| <b>LUMBER</b> (10/7) millions of ft.                    | 451.7#      | 481.2     | -5.9         |
| <b>RAIL FREIGHT</b> (10/7) billions of ton-miles        | 24.9#       | 25.6      | 2.5          |

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA\*, SFPA\*, Association of American Railroads

## PRICES

|                                                             | LATEST WEEK | WEEK AGO | YEARLY % CHG |
|-------------------------------------------------------------|-------------|----------|--------------|
| <b>GOLD</b> (10/18) \$/troy oz.                             | 383.650     | 384.500  | -1.2         |
| <b>STEEL SCRAP</b> (10/17) #1 heavy, \$/ton                 | 140.50      | 140.50   | 5.2          |
| <b>COPPER</b> (10/14) ¢/lb.                                 | 131.1       | 133.8    | 8.6          |
| <b>ALUMINUM</b> (10/14) ¢/lb.                               | 78.5        | 81.5     | -3.4         |
| <b>COTTON</b> (10/14) strict low middling 1-1/16 in., ¢/lb. | 85.10       | 88.41    | 26.8         |
| <b>OIL</b> (10/17) \$/bbl.                                  | 17.64       | 17.28    | 1.4          |

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

## FOREIGN EXCHANGE

|                                | LATEST WEEK | WEEK AGO | YEAR AGO |
|--------------------------------|-------------|----------|----------|
| <b>JAPANESE YEN</b> (10/18)    | 100.66      | 101.01   | 96.88    |
| <b>GERMAN MARK</b> (10/18)     | 1.42        | 1.42     | 1.49     |
| <b>BRITISH POUND</b> (10/18)   | 1.57        | 1.57     | 1.63     |
| <b>FRENCH FRANC</b> (10/18)    | 4.99        | 4.98     | 5.11     |
| <b>ITALIAN LIRA</b> (10/18)    | 1603.1      | 1606.5   | 1527.8   |
| <b>CANADIAN DOLLAR</b> (10/18) | 1.34        | 1.33     | 1.36     |
| <b>MEXICAN PESO</b> (10/18)    | 6.745       | 6.745    | 3.447    |

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

## GROSS DOMESTIC PRODUCT

**Friday, Oct. 27, 8:30 a.m.** ▶ The economy probably grew at an annual rate of 2.2% in the third quarter, according to the median MMS forecast. The projections range from 1.7% to 3.2%, so all economists surveyed expect that growth last quarter was faster than the anemic 1.3% advance of the second period. Consumer and business spending as well as construction added to growth in the summer, suggesting the real final sales continued to grow above 3%. Slower inventory accumulation probably dragged down the GDP gain. The GDP fixed-weight deflator likely rose at an annual rate of 2.7%, little changed from its 2.8% increase in the second quarter.



# This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

## Sunday

IBM is seizing on a new strategy to speed its growth. It's called "network-centric computing," it includes electronic commerce, and you can discuss this Cover Story online with IBM's John M. Whiteside, general manager of IBM Global Network, and BW's Ira Sager, who wrote the story.

**Oct. 22**

**9 p.m. EDT in the Globe**

## Thursday

Interview with the Author: BW's chief economist, William Wolman, talks with Jeffrey Madrick on his new book, *The End of Affluence*, which suggests that the slow growth of the U.S. economy isn't going away—but there are things to do about it. **Oct. 26**

**9 p.m. EDT in the Bowl**

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

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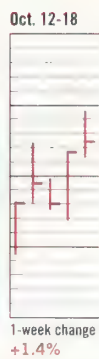
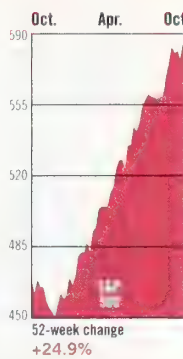
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# Investment Figures of the Week

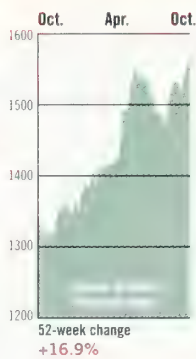
## MARKET COMMENTARY

Rising interest rates sent U.S. stocks soaring. On Oct. 13, the Dow Industrial average climbed to 4794, just short of the 4800 mark as long-term bond yields fell to their lowest level in nearly two years. Traders were reacting to a recent report that consumer spending had risen a bit less than expected in September. But bond prices rose on Oct. 18, as traders expressed concern that the Federal Reserve would not cut interest rates. Technology and financial stocks were strong.

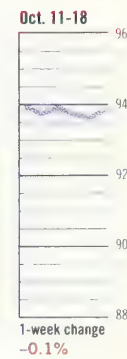
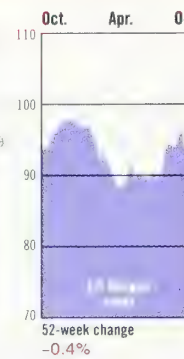
## STOCKS



## BONDS



## THE DOLLAR



## MARKET ANALYSIS

### STOCKS

|                              | Latest | % change |         |
|------------------------------|--------|----------|---------|
|                              |        | Week     | 52-week |
| DOW JONES INDUSTRIALS        | 4777.5 | 0.9      | 21.4    |
| COMPANIES (S&P MidCap Index) | 215.9  | 2.9      | 22.9    |
| COMPANIES (Russell 2000)     | 304.1  | 2.1      | 19.3    |
| COMPANIES (Russell 3000)     | 337.7  | 1.7      | 25.1    |

### INTERNATIONAL STOCKS

|                                 | Latest   | % change (local currency) |         |
|---------------------------------|----------|---------------------------|---------|
|                                 |          | Week                      | 52-week |
| DOW JONES (FINANCIAL TIMES 100) | 3593.0   | 3.4                       | 17.4    |
| NIKKEI INDEX                    | 17,896.0 | 0.0                       | -9.9    |
| DOW JONES (TSE COMPOSITE)       | 4488.9   | 0.3                       | 3.9     |

### FUNDAMENTALS

|                              | Latest | Week ago | Year ago |
|------------------------------|--------|----------|----------|
| 90-DAY TREASURY BILL YIELD   | 5.41%  | 5.45%    | 5.02%    |
| 30-YEAR TREASURY BOND YIELD  | 6.33%  | 6.43%    | 7.89%    |
| S&P 500 DIVIDEND YIELD       | 2.32%  | 2.35%    | 2.75%    |
| S&P 500 PRICE/EARNINGS RATIO | 16.7   | 16.7     | 18.3     |

### TECHNICAL INDICATORS

|                                           | Latest | Week ago | Reading  |
|-------------------------------------------|--------|----------|----------|
| S&P 500 200-day moving average            | 527.7  | 524.6    | Positive |
| Stocks above 200-day moving average       | 69.0%  | 67.0%    | Neutral  |
| Speculative sentiment: Put/call ratio     | 0.64   | 0.75 r   | Neutral  |
| Insider sentiment: Vickers sell/buy ratio | 2.55   | 2.63     | Negative |

BLOOMBERG FINANCIAL MARKETS

## INDUSTRY GROUPS

### MONTH LEADERS

|                          | % change |          |
|--------------------------|----------|----------|
|                          | 1-month  | 12-month |
| PHARMACEUTICALS          | 12.7     | 59.3     |
| COMPUTER SYSTEMS         | 7.5      | 39.9     |
| TELECOMMUNICATIONS       | 7.2      | -15.6    |
| CONSUMER ELECTRONICS     | 7.0      | 51.4     |
| RETAIL APPAREL RETAILERS | 6.8      | 2.8      |

### Strongest stock in group

|                   | % change |          | Price  |
|-------------------|----------|----------|--------|
|                   | 1-month  | 12-month |        |
| PFIZER            | 17.9     | 62.5     | 58 1/2 |
| DIGITAL EQUIPMENT | 22.1     | 69.4     | 49 3/4 |
| U.S. HEALTHCARE   | 10.5     | -23.0    | 35 1/8 |
| LORAL             | 9.4      | 49.4     | 29 1/8 |
| TIJX              | 24.0     | -11.9    | 14 1/8 |

### MONTH LAGGARDS

|                            | % change |          |
|----------------------------|----------|----------|
|                            | 1-month  | 12-month |
| GLASS AND GLASS CONTAINERS | -19.6    | -9.0     |
| PACKAGING                  | -14.5    | -14.5    |
| TOOLING                    | -12.3    | -0.2     |
| CONTAINERS                 | -12.1    | -7.5     |
| RETAIL MERCHANDISE CHAINS  | -11.1    | 0.3      |

### Weakest stock in group

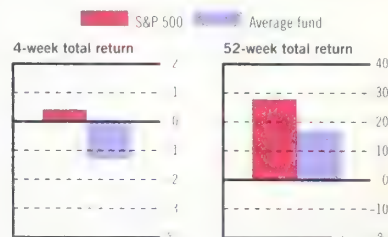
|                     | % change |          | Price  |
|---------------------|----------|----------|--------|
|                     | 1-month  | 12-month |        |
| CROWN CORK & SEAL   | -19.8    | -9.9     | 35 3/8 |
| ROADWAY SERVICES    | -20.3    | -21.5    | 43 1/4 |
| CINCINNATI MILACRON | -20.5    | -2.3     | 26 1/4 |
| STONE CONTAINER     | -17.1    | -13.0    | 17 1/8 |
| KMART               | -28.8    | -34.9    | 10 1/2 |

## MUTUAL FUNDS

MORNINGSTAR INC.

### LEADERS

|                                 | %    | LAGGARDS                            | %     |
|---------------------------------|------|-------------------------------------|-------|
| 4-week total return             |      | Four-week total return              |       |
| DOW JONES INDUSTRIAL INDEX      | 6.0  | WRIGHT EQUIFUND-MEXICO              | -18.4 |
| TELECOM-RUSHMORE UTILITY INCOME | 5.5  | FIDELITY SELECT DEVELOPING COMMUN.  | -10.3 |
| PHARMACEUTICALS                 | 4.9  | RESERVE INFORMED INVESTORS GROWTH   | -10.1 |
| 52-week total return            |      | 52-week total return                |       |
| DOW JONES INDUSTRIAL INDEX      | 87.8 | WRIGHT EQUIFUND-MEXICO              | -57.3 |
| FIDELITY SELECT ELECTRONICS     | 72.0 | BT INVESTMENT LATIN AMERICAN EQUITY | -40.8 |
| FIDELITY SELECT COMPUTERS       | 71.1 | TCW/DW LATIN AMERICAN GROWTH        | -40.7 |



## RELATIVE PORTFOLIOS

DR/M-GRAW HILL

Relative portfolios represent the performance of a \$10,000 investment one year ago. The numbers indicate the total returns.

**Treasury bonds**  
\$12,968  
+1.79%

**U.S. stocks**  
\$12,729  
+1.60%

**Foreign stocks**  
\$10,774  
+0.25%

**Money market fund**  
\$10,550  
+0.12%

**Gold**  
\$9,781  
-0.44%

Figures on this page are as of market close Wednesday, Oct. 18, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are

as of market close Oct. 17. Mutual fund returns are as of Oct. 13. Relative portfolios are valued as of Oct. 17. A more detailed explanation of this page is available on request. r=revised



# MERGERS: WILL THEY EVER LEARN?

**H**ere they go again. Yet another wave of merger mania is sweeping through Corporate America. The value of all announced deals in the first nine months of this year hit \$248.5 billion, passing the record full-year total of \$246.9 billion for 1988, according to Mergerstate, a merger research service. And this time it's different, right? These acquisitions are not like the conglomerates of the '60s, which have since broken up. They're not like the debt-laden leveraged buyouts of the '80s, most of which didn't fare any better. No, these are strategic deals, designed to be smart, friendly, full of synergy, and great for shareholders.

Don't bet on it. Despite the hype about vertical integration, economies of scale, better distribution channels, and more market clout, the current wave of mergers may be enriching investment bankers more than stockholders. A new study by BUSINESS WEEK and Mercer Management Consulting Inc. of 150 deals worth \$500 million or more completed in the first half of this decade shows that about half destroyed shareholder wealth, judged by stock performance in relation to Standard & Poor's industry indexes. Another one-third barely contributed anything at all (page 122).

Why are so many recent mergers capital-killers? First, most companies aren't good at making acquisitions. They don't have the experience. Their biggest mistake is not following through. Successful mergers are made after the deal is signed by combining corporate cultures and bureaucracies—an art form mastered by only a few. Many companies simply pay much too much for an acquisition. Others have misplaced notions about that chimera, synergy. Entertainment and drug companies are paying huge bucks for distribution. But will they get locked in and lose flexibility?

Finally, there is the matter of CEO ego. Many mergers are driven by management emotion—trying to be the biggest, wanting to best a rival. Synergy is the rationalization. Harvard University's Michael Porter says that CEOs like mergers because "it's the big play, the dramatic gesture."

Better to leave that kind of ego on the golf course. Done correctly, mergers and acquisitions are good for companies, stockholders, and the economy. But too many today are being done for the wrong reasons. Shareholders beware.

# LET'S JUST FIRE THE SPIES

**T**he CIA appears to be having the same kind of success with economic spying on U.S. allies as it had spying on its enemies. In the case of the old Soviet Union, intelligence estimates of the size of its economy in the 1970s and 1980s were wildly inflated. Economic spying on Japan and France recent-

ly is proving equally unproductive. Japan got everything it wanted in this past summer's auto talks, despite electronic eavesdropping by U.S. intelligence agents on its negotiating team. And French counter-intelligence agents set up a sting for CIA operatives trying to "get" Paris' position on agricultural General Agreement on Tariffs & Trade talks. The American economic spies were unceremoniously booted out.

The plain fact is that spying on allies is neither an ethical nor an efficient means of gathering economic information. Most information is already freely available to the public. A systematic search of databases and in-depth interviewing of public officials can provide an accurate economic picture of any country. The Japanese have excelled at this for decades.

Since the end of the cold war, U.S. intelligence agencies have been searching for a new role. With a \$30 billion budget, they have to show Congress a reason for being. The Clinton Administration has come to the rescue by making economic intelligence a new priority. This is a mistake. For a fraction of the sum spent on spying, Washington can gather data by using foreign-speaking analysts to comb public documents.

The U.S. should simply cut its oversized spying budget and stop trying to get Jack Ryan to play Alan Greenspan.

# A LABOR AGENDA FOR THE '90s

**I**n the past two decades, the U.S. labor movement has been in the pits. Battered by global competition, technological change, hostile employers, and a more conservative political environment, most labor leaders have been all too willing to lament their fate rather than change it. Now, a group of reformers is poised to take over leadership of the AFL-CIO. Led by Service Employees' International Union President John J. Sweeney and United Mineworkers President Rick L. Trumka, the group has already ousted longtime federal President Lane Kirkland, who did little for 16 years.

But how reformist are the reformers? The new agenda for aggressive membership drives in low-wage industries using old-fashioned 1930s-style tactics such as strikes and picketing, plus some new ones, such as filing federal lawsuits against mergers. The unions plan to rebuild their political muscle by remaking their image with workers and the public.

But is this a labor plan for the new millennium? We doubt it. In a global marketplace, higher wages accrue to the most skilled, most educated. The big challenge for Sweeney and Trumka is to raise the value of America's workers. Sweeney says he favors cooperation with management toward this end, but must also find a way to improve training. Finally, it will help if Sweeney got some labor leaders to end their perquisites, such as huge salaries and their own jets.

A stronger labor movement could benefit American society. Unions historically have provided a means for workers to improve their middle class, and labor's decline may be one of many reasons the gap between rich and poor has widened. But unions, and their leaders, have to remake themselves.



OW TERRY HOOPER MADE THE WISE DECISION

TO DUMP HER STOCK IN THE MIDDLE OF A LAKE.



**8:21 A.M.**

*The lake makes for a well deserved break. A page from her broker informs that the risky stock purchase opened at 7 7/8.*

**10:46 A.M.**

*Bad news. After sitting on her sunglasses, she sees that it dropped to 5 3/4.*

**12:27 P.M.**

*Sell quickly to avoid a total loss? No, she digs her feet into the soft sand and waits. It climbs back to 7.*

**2:42 P.M.**

*The fluctuating stock jumps and she sells before the bottom drops out. A relaxing day has turned a small profit financially, and a big one mentally.*

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it that far. Imagine an automobile that impresses you with both its interior room (m

















